

Regional Economic Report

October - December 2012

Summary

During the fourth quarter of 2012 the regional economies are estimated to have expanded at a pace that was moderate compared to the one observed in the first half of the year. Thus, the deceleration in economic growth, which was first noticed in the north and in the south in the previous quarter, extended to the central regions. The slowdown in most regional economies was driven by an incipient weakening of the services' sector, as well as by the modest performance of the construction industry. Furthermore, in the center and in the south manufacturing production contracted. On the other hand, in the context of more favorable weather conditions with respect to the same period of the previous year, when severe drought was registered, the agricultural production recovered in all the regions.¹

Annual headline inflation resumed its trend towards the 3 percent permanent target during the fourth quarter of 2012 in the four regions in which Mexico is divided for the purposes of this Report. After persisting for several months above 4 percent in all the regions –Northern, North-Central, Central and Southern– it situated below this mark in December 2012 and at the beginning of 2013. This performance was driven by the partial fading away of the shocks that had previously affected the short-term trajectory of inflation –which confirmed that their nature, just as anticipated by Banco de México, was transitory and would not affect the general price formation process in the economy. It is noteworthy that annual core inflation, which is an indicator of the medium-term trend of annual headline inflation, decreased in the reference period in all the regions. Thus, by the end of the fourth quarter of 2012 and the beginning of 2013, this variable located at levels close to 3 percent in the Central and the Southern regions, and in the Northern one it lied at even lower levels, near 2 percent.

The business agents interviewed by Banco de México in all regions during December 2012 and January 2013 mostly estimated that the regional economies will continue growing over the next six and twelve months. Nonetheless, they considered that economic growth will keep decelerating during the first part of 2013 –which they consider could be more pronounced in the north, and, at the sectoral level, in the manufacturing industry. The economic dynamism of the regions, according to the interviewed business contacts, will rely to a large extent on domestic demand, on investment in certain industries, such as the automobile and the

mining industries, and on infrastructure works which would contribute to enhancing productivity.

In relation to the abovementioned, as well as to the agenda adopted by Banco de México in this Regional Economic Report, two Boxes analyzing the drivers of regional economic growth have been included in this Report. The first Box discusses the results of a survey of businesses on the impact of the labor reform at the regional level; according to this survey, firms expect that the labor reform will contribute to a greater incorporation of the labor force into the economy's formal sector, anticipating this to occur nationwide. The second Box analyzes the regional differences in the labor productivity of the manufacturing industry and its relation to the infrastructure endowment. The results imply that the development of greater public infrastructure will contribute to enhancing labor productivity in the manufacturing industries of all the regions.

Business agents interviewed by Banco de México acknowledged that their forecasts regarding the expansion of economic activity in 2013 could be affected depending on the realization of certain external and domestic risks. In this respect, they considered that regarding external risks the concern over a lower than expected world rate of economic expansion remained widespread. They also indicated that downside domestic risks prevail, two of them standing out: first, the vulnerability of public finances at the state and municipal level and its potential impact on public works; and, second, a reversal of the progress achieved so far in perceived public safety. Despite these risks, a great number of these business agents pointed out that the process of structural reforms in Mexico would contribute to strengthening the potential for economic growth.

Regarding inflation, the business contacts interviewed by Banco de México for this Report specified that lower inflationary pressures were anticipated for 2013 as compared to 2012. This is in line with the expectation of smaller annual percentage increases in commodity prices and in salary costs. Likewise, they mentioned that the expected moderation in the growth of own products and services' prices is partly due to the environment of intensified market competition they are presently going through.

¹ Regionalization: Northern: Baja California, Sonora, Chihuahua, Coahuila, Nuevo León and Tamaulipas; North-Central: Aguascalientes, Baja California Sur, Colima, Durango, Jalisco, Michoacán, Nayarit, San Luis Potosí, Sinaloa and Zacatecas; Central: Distrito Federal, Estado de México, Guanajuato, Hidalgo, Morelos, Puebla, Querétaro and Tlaxcala; and Southern: Campeche, Chiapas, Guerrero, Oaxaca, Quintana Roo, Tabasco, Veracruz and Yucatán.