Boosting Sustainable Economic Growth in Mexico
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Since the middle of 2009, Mexico has been experiencing a process of continuous economic recovery.
The current upturn has been balanced, including domestic fixed investment and consumption.

**Investment**

2007 = 100; s.a.

s.a. / Seasonally and trend-adjusted

Source: Mexico’s National Accounts System, INEGI

**Retail Sales**

2007 = 100; s.a.

s.a. / Seasonally and trend-adjusted

Source: Commercial establishment survey, INEGI
The domestic economic rebound has been possible thanks to Mexico’s macroeconomic fundamentals

- Contained public debt with rising average maturity
- Relatively low inflation
- Well-capitalized, provisioned, and liquid banking system
A positive feedback loop has emerged between labor market developments, bank lending and consumer spending.

**Employment and Unemployment**

- Million workers
- % EAP
- Unemployment (right)
- Employment (left)

*Workers insured by the Mexican Social Security Institute (IMSS) and unemployed people relative to Economically Active Population (EAP)*

s.a. / Seasonally adjusted

Source: IMSS and INEGI

**Consumer Bank Performing Loans**

2007=100

Source: Banco de México
Extraordinary support has been provided by external conditions, particularly from advanced countries

- On the surface this may sound contradictory
- Two positive factors
  - Demand for Mexican exports
  - Unusually favorable financing conditions
Manufacturing exports have been increasing, although with some recent moderation.

**Manufacturing Exports by Destination**

2007=100; s.a.

- Red: Total
- Purple: U.S.
- Green: Others

**Industrial Production**

2007=100; a. e.

- Blue: U.S.
- Red: Mexico

s.a. / Seasonally and trend-adjusted

Source: Banco de México

* / U.S. and Mexico’s correlation is close to 0.9

Source: INEGI
Monetary easing abroad has translated into domestic interest rates at or close to all-time lows

Foreign Holdings of Peso Government Bonds
% of Local Government Bonds held by Foreigners in EM¹

Yield Curve
%

1/ Include Brazil, Hungary, India, Indonesia, Malaysia, Mexico, Poland, Thailand and Turkey
Source: Barclays

* / October 26, 2012
Source: Banco de México
The most serious risk associated with capital inflows is not the ever-present possibility of a reversal

- A “sudden stop” may occur for reasons not exclusively related to the recipient country
- The most serious risk is ignoring the likelihood of the event
  - Financial crises emerge because people assume that easy credit will last forever
- Possible capital reversal calls for prudence
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The base-case scenario for Mexico’s economic outlook assumes the continuation of favorable external conditions.

### GDP Outlook

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<th>2012&lt;sup&gt;F&lt;/sup&gt;</th>
<th>2013&lt;sup&gt;F&lt;/sup&gt;</th>
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<tr>
<td>Mexico</td>
<td>3.9</td>
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<sup>F</sup> Forecast

Source: Consensus Forecasts, Latin America Consensus Forecasts and Asia Consensus Forecasts; October 2012
Significant external risks relate to the developments in the United States and Europe

Risks

United States

- The “Fiscal Cliff” could lead to a fall of 0.3% in GDP in 2013\(^1\)
- As industrial production in the U.S. slows, the impact on the Mexican economy could be significant\(^2\)

Europe

- The difficulty in resolving underlying problems could generate new bouts of volatility and risk aversion

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Annual inflation has been rising mainly as a result of agricultural price pressures

Consumer Price Index
Annual; %

* First half
Source: INEGI
However, core inflation has also been increasing.

Core Price Indices
Annual; %

* First half
Source: INEGI
Monetary policy will have to be adjusted in a timely way if convergence of inflation to the 3% target is endangered

- Need to evaluate whether current price pressures are transitory
- Two sources of risk should be especially monitored
  - Amplification of second-round effects from external shocks
  - Aggregate demand pressures
- The most essential challenge continues to be the anchoring of inflation expectations on the 3% permanent target
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Concluding remarks

- The ongoing economic recovery does not imply that the economy is growing at rates that are sufficient to meet social needs or exploit potential opportunities.
- Mexico needs to consolidate macroeconomic stability.
- Additionally, total factor productivity growth should be facilitated.
- Considerable efficiency gains seem possible in the services sector and in non-manufacturing industries.
- Remove obstacles in order to reduce informality and facilitate competition.
Mejoran las perspectivas económicas mundiales