Regional Economic Report
July – September 2023
Summary

FOREWARNING: This document is provided for the reader's convenience only. The translation from the official Spanish version was made by Banco de México's staff. Discrepancies may arise between the original document in Spanish and its English translation. For this reason, the original Spanish version is the only official document.

During the third quarter of 2023, economic activity in Mexico continued expanding and maintained robust growth. Its evolution during the quarter reflected the good performance of tertiary activities, which grew at a faster rate compared to the previous quarter, as well as the dynamism of industrial activity, which was supported by the strong growth of non-residential construction.

At the regional level, economic activity is expected to have continued expanding in all regions during the reported quarter.[1] Certain tertiary activities, such as trade and tourism, are anticipated to have contributed to this favorable performance. In addition, spending on construction increased in all regions, especially in the Southern one. Other industrial activities, such as manufacturing in the Northern and North-Central regions, and mining in the Central region are estimated to have also supported regional growth. Agricultural and livestock production are also expected to have contributed to the increase of economic activity in the Central and Southern regions.

To complement the analysis of the recent evolution of regional economic activity, the results in Box 1 suggest that regional exports were influenced heterogeneously by changes in US demand generated by adjustments in the sectoral composition of US imports, or by changes in Mexico's relevance as a supplier of goods to the United States. In this regard, these variations in external demand are estimated to have had a positive impact on the value added of all regions.

Annual headline inflation decreased in all regions between the second and third quarter of 2023. This behavior was associated, to a greater extent, with the decline in annual core inflation in all regions, although non-core inflation also decreased between quarters. In all regions, within the core component, annual merchandise inflation continued trending downwards. In contrast, annual services inflation still does not show a clear downward inflection point.

To analyze the behavior of consumer prices in greater detail, Box 2 illustrates that increases in core inflation levels have been heterogeneous across the Mexican regions. These differences can be explained by both different pressures on their prices and differences in the weights used to calculate regional inflation. For example, for most of the period between 2020 and 2022, core inflation in the Southern region was above the national one. This is partially attributed to the fact that its consumption basket is mostly oriented towards goods (compared to the rest of the regions), which increased more than services at the beginning of the pandemic. Box 3 shows that, despite the significant increase in food prices between 2018 and 2022, extreme poverty by income decreased in most regions in that period, which was especially noticeable in the Southern region, which has historically exhibited the highest poverty levels. This was due to both the real growth in per capita income and a more favorable distribution of income for poverty reduction, as both factors compensated for the significant increase in the cost of the basic food basket. Box 4 evaluates the degree of spatial integration between Mexican and US markets

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

through the analysis of price indices in several cities in both countries. The results confirm the spatial integration in both countries' tradable goods markets, at least to some extent. However, this result does not hold in the case of non-tradables, particularly in education and housing services.

Based on information gathered during the program of interviews with business agents, in all regions, the diffusion indices of expectations for the demand for products they offer, for personnel hired and for investment in fixed assets, for the next twelve months remained in the expansion zone. In the reported quarter, demand expectations strengthened in the Northern region, while those for employment and investment did so in the Southern one.

The interviewed business agents highlighted the following risks to regional economic growth. On the downside: i) that public safety indicators deteriorate; ii) that uncertainty generated by the 2024 elections, common in these types of processes, is higher than expected; iii) that inflation persists at high levels, and iv) that severe weather phenomena adversely impact regional economic activity. Among upside risks, they mentioned: i) that public spending, particularly investment in infrastructure projects, is higher than expected, and ii) that more favorable conditions are observed, both domestically and internationally, thus promoting higher levels of private investment.

In the Northern, North-Central, and Southern regions, there was a reduction in the percentage of responses from interviewed business agents anticipating the selling prices of the goods and services they offer to increase at a slower rate, to remain unchanged, or to decrease over the next twelve months, which interrupts the sequence of increases in said percentage that had been observed in 2023. Regarding input prices, the proportion of business agents expecting them to grow at a higher or similar rate also increased in most regions. Moreover, more than half of interviewed business agents in all regions anticipate wage costs to increase at a higher or similar rate in the next twelve months compared to the previous twelve months.

Looking ahead, regional economies are anticipated to continue expanding, despite facing a complex and uncertain environment that poses significant challenges to their growth. Among these challenges, the possibility of an economic slowdown in the United States is considered, which could particularly impact states in the Northern and Central regions that are clearly export-oriented. Likewise, adverse weather events may affect the performance of those Mexican states that are most vulnerable to such phenomena, as recently evidenced by the impact of Hurricane Otis in Acapulco, Guerrero. To address these and other similar challenges, it is crucial to implement measures that generate favorable conditions for investment and strengthen the factors that influence regional growth in an inclusive and sustainable manner.