

Mexico

Mexico Economy Expands in First Quarter; Fourth Quarter Revised Higher

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Mexico's economy grew solidly in the first quarter despite higher inflation, interest rates and uncertainty over trade relations. Gross domestic product (GDP) expanded at a 2.4 percent annualized rate, while fourth-quarter output was revised higher to 2.9 percent. The consensus 2017 GDP growth forecast was revised up from 1.5 percent to 1.7 percent. Recent data on exports, industrial production, retail sales and employment showed continued expansion but at a slower pace. Inflation increased, but the peso recovered some ground against the dollar in April for a third consecutive month.

Output Growth Solid

Mexico's GDP grew at a 2.4 percent annualized rate in the first quarter, with activity mostly driven by service sector growth (*Chart 1*). Service-related activities (wholesale and retail trade, transportation and business services) rose 4 percent, while goods-producing industries (manufacturing, construction, utilities and mining) were flat. Agricultural output grew 2.8 percent in the first quarter. Fourth-quarter GDP growth was revised higher from 2.4 percent to 2.9 percent.

Export Growth Slowing

Exports rose 0.4 percent in March after growing 3.4 percent in February; however, the three-month moving averages of total and manufacturing exports fell in March, suggesting some slowing after consistent increases since mid-2016 (*Chart 2*). Total exports are up 8 percent year to date through March relative to the same period in 2016. Manufacturing exports grew 6 percent. Oil exports turned around earlier in 2016 after a long decline and rose 56 percent in the first three months of 2017.

Industrial Production Steady

Mexico's industrial production (IP) grew 0.1 percent in both February and January, while manufacturing production was flat in February after growing 0.5 percent in January. U.S. IP rose 0.6 percent in March after no growth in February. Based on the three-month moving average, Mexico's manufacturing IP has accelerated while total IP shows signs of stabilizing (*Chart 3*). Total IP, which includes manufacturing, construction, oil and gas extraction, and utilities, has grown more slowly than manufacturing IP since 2014.

Retail Sales Growth Moderating

Retail sales rebounded, expanding 2.4 percent in February after falling in January and December. February sales were up 7.6 percent year over year. Nevertheless, the

Chart 1
First-Quarter Growth Solid While Fourth Quarter Revised Higher
Quarterly percent change, annualized

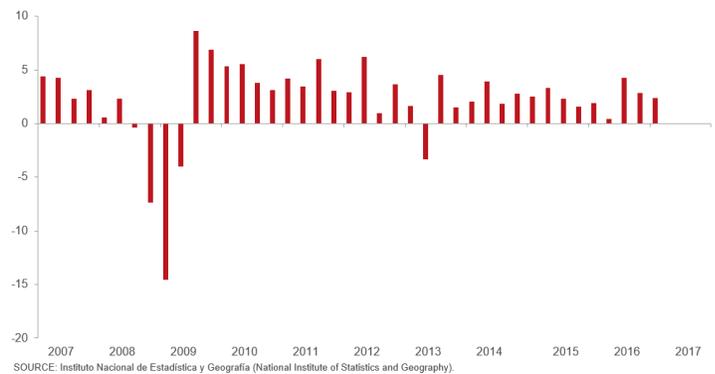


Chart 2
Moving Average of Exports Dips
Index, January 2000 = 100*

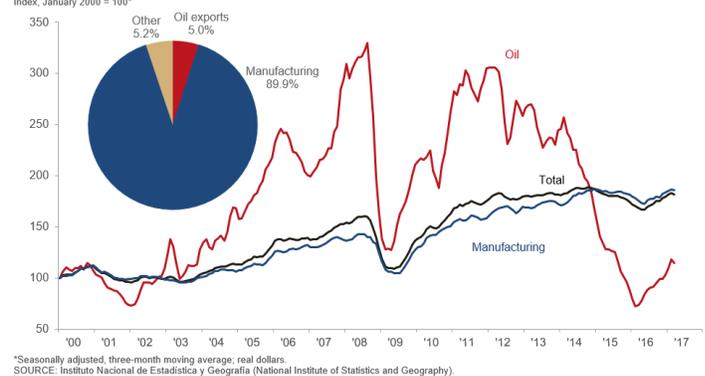
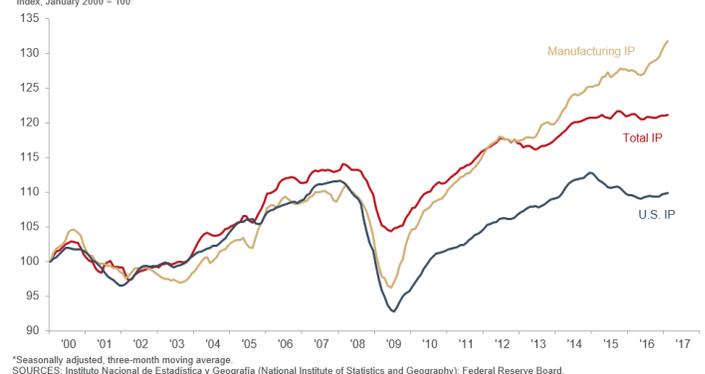


Chart 3
Industrial Production Stabilizes as Manufacturing Production Continues Steep Rise
Index, January 2000 = 100*



smoothed retail sales data (three-month moving average) fell in February for the first time since late 2015 (*Chart 4*). A sharp increase in fuel prices in January, part of the government's plan to remove fuel subsidies, is expected to weigh on consumer spending this year. Despite this, the consumer confidence measure improved in April and March.

Job Growth Remains Robust

Formal-sector employment—jobs with government benefits and pensions—grew at an annualized rate of 5.7 percent in March, after expanding 4.4 percent in February (*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 April

The Mexican currency continued to strengthen in April, averaging 18.8 pesos per dollar—a 14 percent gain from January (*Chart 6*). The peso remained 7 percent lower against the dollar on a year-over-year basis. The Mexican currency initially weakened last year in anticipation of increases in U.S. interest rates as well as policy and economic uncertainty following the U.S. presidential election.

Chart 4
Retail Sales Growth Eases in 2017

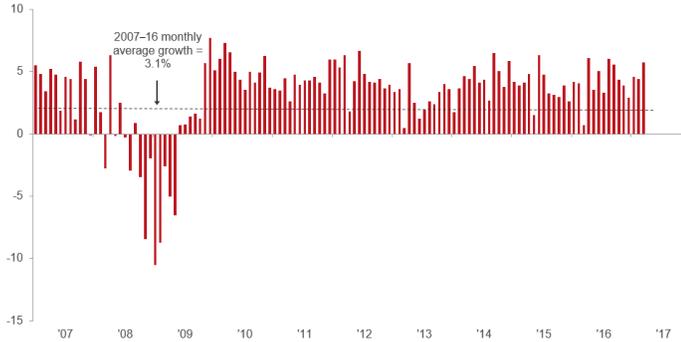
Index, January 2000 = 100*



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

Chart 5
Job Growth Robust So Far in 2017

Percent*



*Month/month, seasonally adjusted, annualized rate.
SOURCE: Instituto Mexicano del Seguro Social (Mexican Social Security Institute).

Chart 6
Peso Continues Its Recovery Against the Dollar in April

Peso/dollar average



SOURCE: Banco de México.

Foreign-Owned Government Debt Stable

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

Inflation Ticks Up in April

Annual inflation inched up to 5.8 percent in April, compared with 5.4 percent in March—significantly above Banco de México's long-term target of 3 percent (*Chart 8*). Core inflation (excluding food and energy) rose 4.5 percent over the 12 months ended in April. Mexico's central bank raised its benchmark interest rate by 25 basis points in March, to 6.5 percent, the eighth increase since December 2015. Banco de México Governor Agustín Carstens has stated that the central bank will use interest-rate increases and currency interventions as needed to strengthen the peso and stabilize prices.

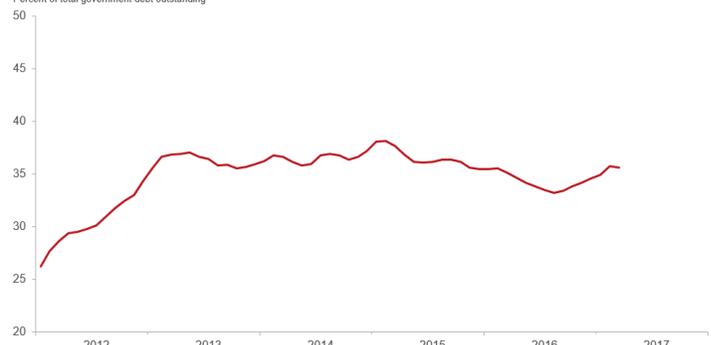
—Jesus Cañas

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

Percent of total government debt outstanding*



*Three-month moving average.
SOURCE: Banco de México.

Chart 8
Inflation Remains High in April

12-month percent change



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