

Mexico Economy Continues Expanding in Second Quarter

August 8, 2017

Mexico's economy posted solid growth in second quarter 2017, although gross domestic product (GDP) growth ticked down slightly from the first quarter, according to the government's advance estimate. Recent data on exports, industrial production and employment improved, but retail sales fell. Inflation held steady in June as the peso gained ground against the dollar for the fifth consecutive month. The consensus 2017 GDP growth forecast was unchanged at 2 percent.

Output Growth Continues in Second Quarter

Mexico's GDP grew 2.4 percent annualized in the second quarter, a slightly slower pace than the 2.7 percent in the first quarter (*Chart 1*). Activity in the second quarter was mostly driven by growth in the service sector (including trade, transportation and business services), which rose 3.2 percent. Goods-producing industries (including manufacturing, construction, utilities and mining) grew only 0.4 percent, while agricultural output dipped 8 percent in the second quarter.

Exports Edge Up in May after April Decline

Total exports grew 0.9 percent in May after falling 2.2 percent in April. Recent deceleration in export growth, however, is apparent in the three-month moving average (*Chart 2*). Total exports are up 7.8 percent year to date through May relative to the same period in 2016. Manufacturing exports grew 6.3 percent, and oil exports were up 34.4 percent in the first five months of 2017, compared with the same period a year ago.

Industrial Production Sluggish

Mexico's industrial production (IP), which includes manufacturing, construction, oil and gas extraction, and utilities, grew 0.1 percent in May after falling for three consecutive months. Manufacturing IP fell 0.3 percent in May after expanding 0.6 percent in April.

The three-month moving average of total IP has dipped in recent months, while manufacturing IP has been flat (*Chart 3*). In the U.S., IP rose 0.1 percent in May after increasing nearly 1 percent in April.

Retail Sales Flat

May retail sales slipped 0.1 percent after expanding 1.2 percent in April. While the latest sales figure represents an increase of 3.4 percent year over year, the three-month moving average shows increased volatility and essentially no growth in 2017 after a prolonged upward trend that began in late 2015 (*Chart 4*). Consumer confidence in June worsened after four months of continued improvement.

Chart 1
Second-Quarter Gross Domestic Product Growth Robust

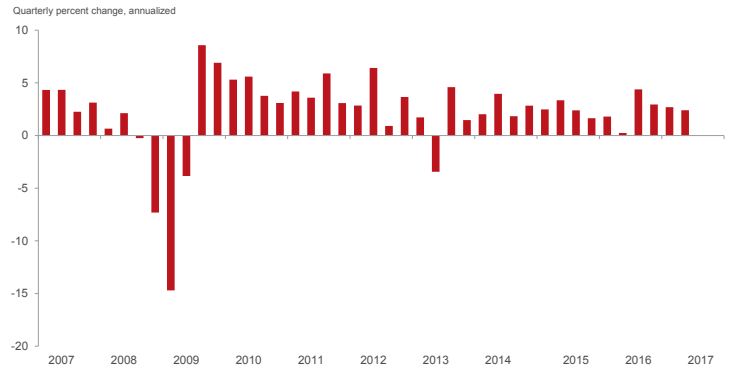


Chart 2
Export Growth Slows in Second Quarter

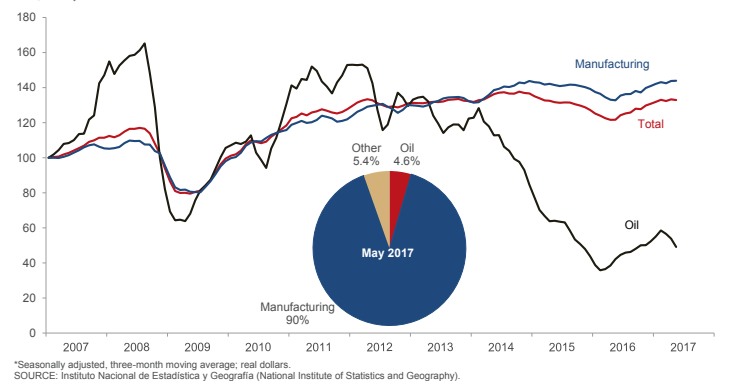
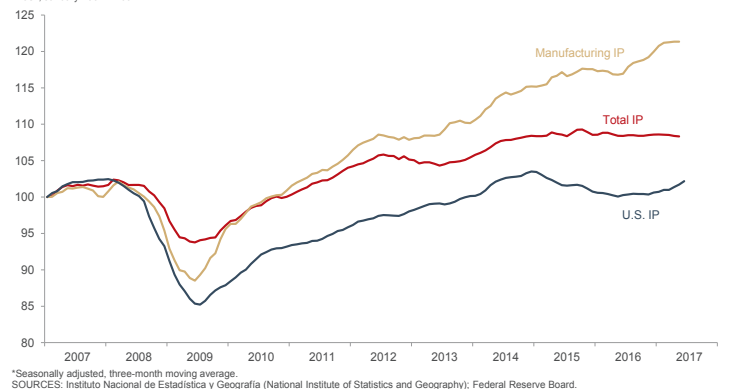


Chart 3
Manufacturing Production Growth Slows

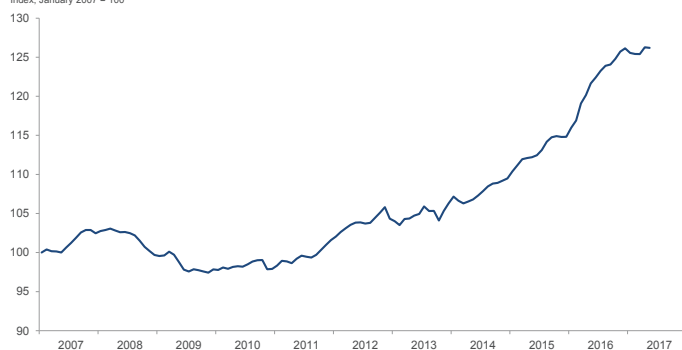


Job Growth Maintains Strong Pace

Formal-sector employment—jobs with government benefits and pensions—grew at an annualized rate of 4.8 percent in

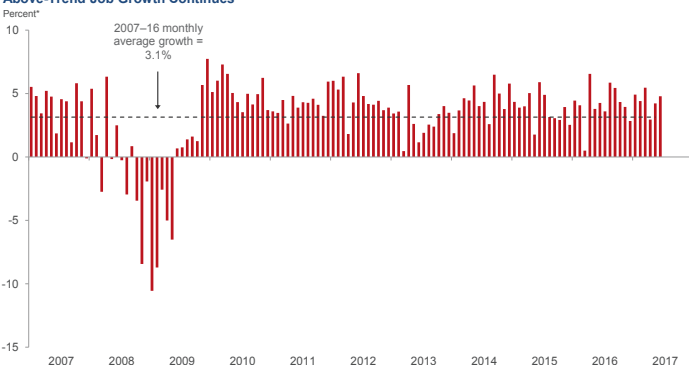
Chart 4
Retail Sales Stall Following Prolonged Strength

Index, January 2007 = 100*



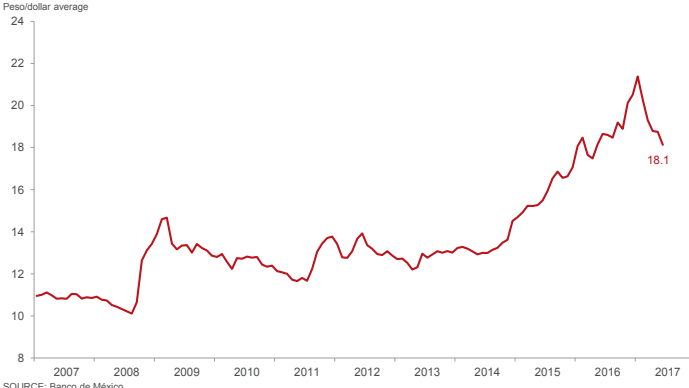
*Seasonally adjusted, three-month moving average; real pesos.
SOURCE: Instituto Nacional de Estadística y Geografía (National Institute of Statistics and Geography).

Chart 5
Above-Trend Job Growth Continues



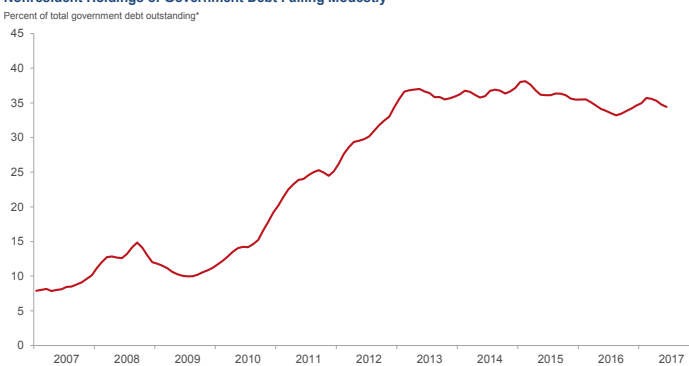
*Month/month; seasonally adjusted, annualized rate.
SOURCE: Instituto Mexicano del Seguro Social (Mexican Social Security Institute).

Chart 6
Peso Continues Strengthening Against the Dollar



SOURCE: Banco de México.

Chart 7
Nonresident Holdings of Government Debt Falling Modestly



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

June after expanding 4.2 percent in May (*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 June

The Mexican currency averaged 18.1 pesos per dollar in June, a 3.4 percent gain from May (*Chart 6*). The peso is up 18 percent since January and is practically back to its level seen a year ago. 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.

Foreign-Owned Government Debt Trending Slightly Downward

With stabilization of the peso/dollar exchange rate, the share of peso-denominated government debt held abroad has declined in recent months (*Chart 7*). This debt share has hovered near 35 percent year to date. 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 Holds Mostly Steady in June

Annual inflation ticked up, reaching 6.3 percent in June compared with 6.2 percent in May—still significantly above Banco de México’s long-term target of 3 percent (*Chart 8*). Core inflation (excluding food and energy) rose 4.8 percent over the 12 months ending in June. Mexico’s central bank raised its benchmark interest rate by 25 basis points to 7 percent, the 10th 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 and Alexander T. Abraham

About the Authors

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

Chart 8
Inflation Continues to Be Significantly Above Target in June



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