

Overview of the Mexican Economy

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U.S.-Mexico Manufacturing: Back in the Race

Federal Reserve Bank of Dallas, El Paso Branch

October 9th, 2015

I

External Conditions

II

Inflation

III

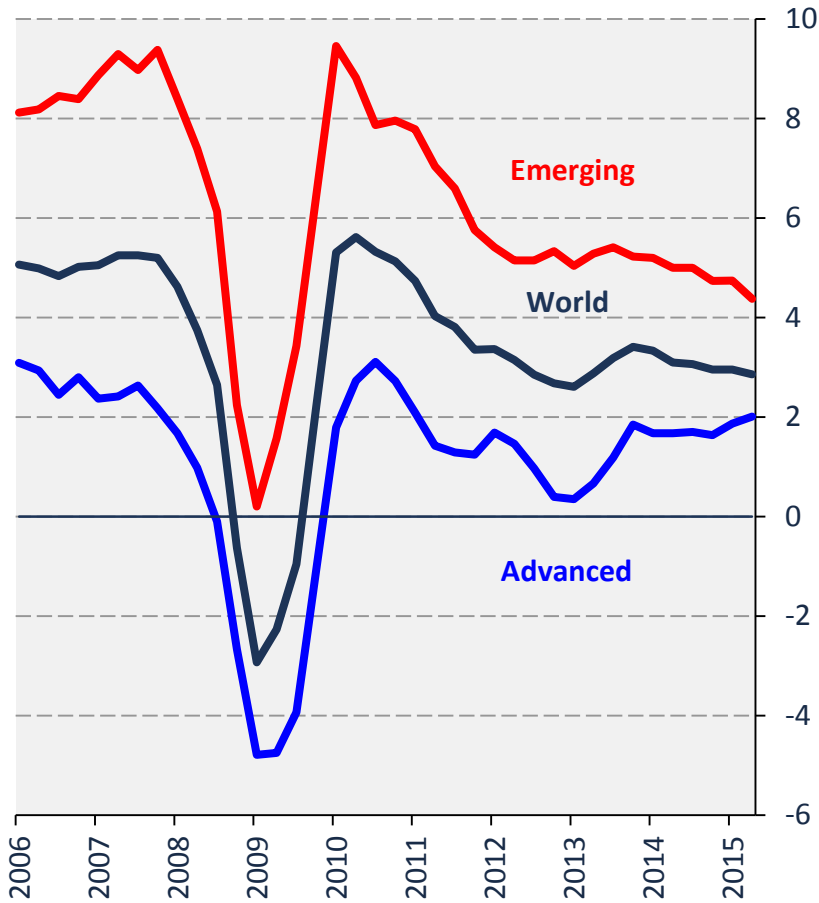
Economic Activity

IV

Outlook and challenges

The international economic environment has become even more challenging. In particular, global economic growth has been lower than expected.

World GDP Growth
Annual percentage change, s. a.

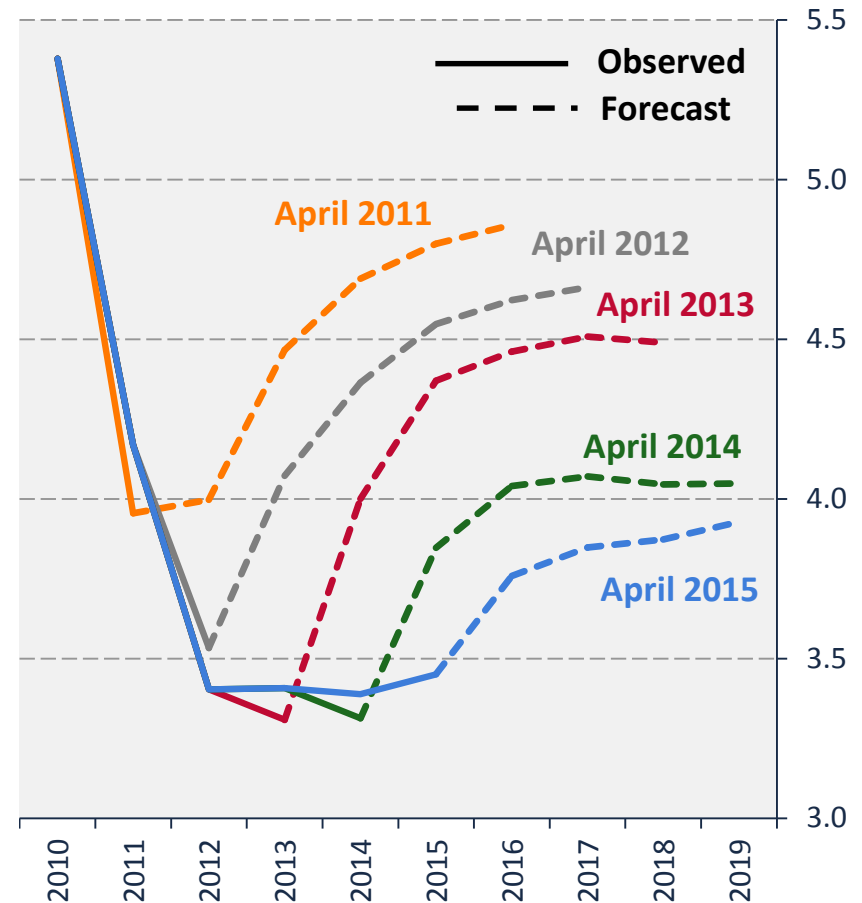


s. a./ seasonally adjusted.

Note: The sample of countries represents 86.1% of the world's GDP measured by purchasing power parity.

Source: Elaborated by Banco de México with data from Haver Analytics.

Global Economic Growth Forecasts
Annual percentage change



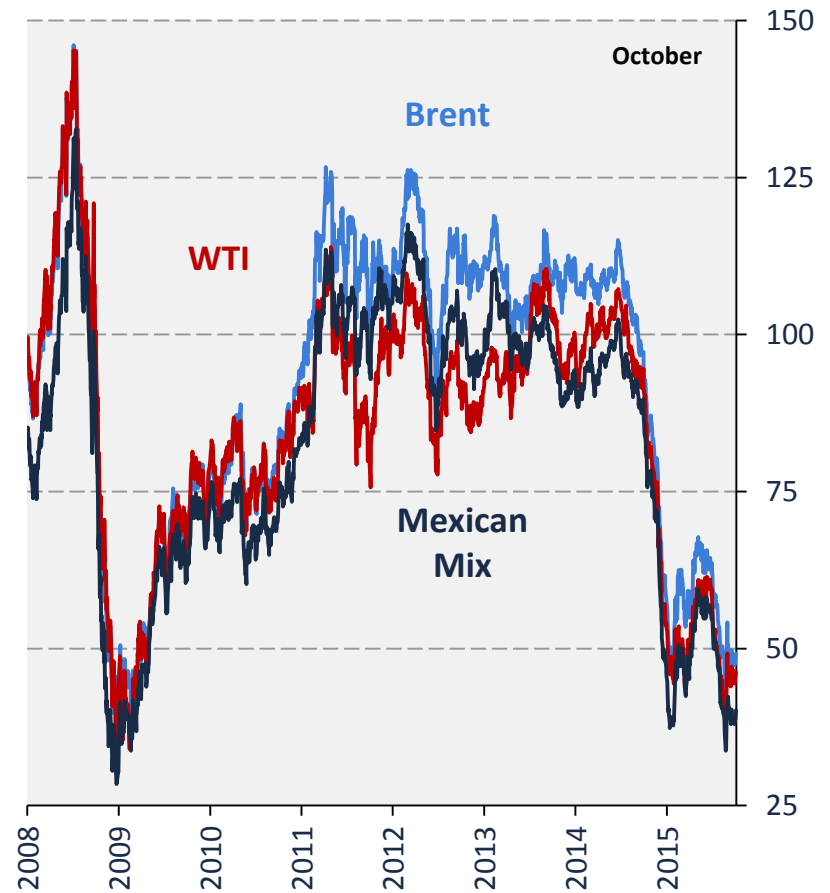
Source: IMF.

Commodity prices, particularly oil prices, are well below the levels seen in recent years and are expected to remain low.

CRB^{1/} Commodities Index
Index 31-dic-2007=100



Evolution of Selected Crude Oil Prices
Dollars per barrel



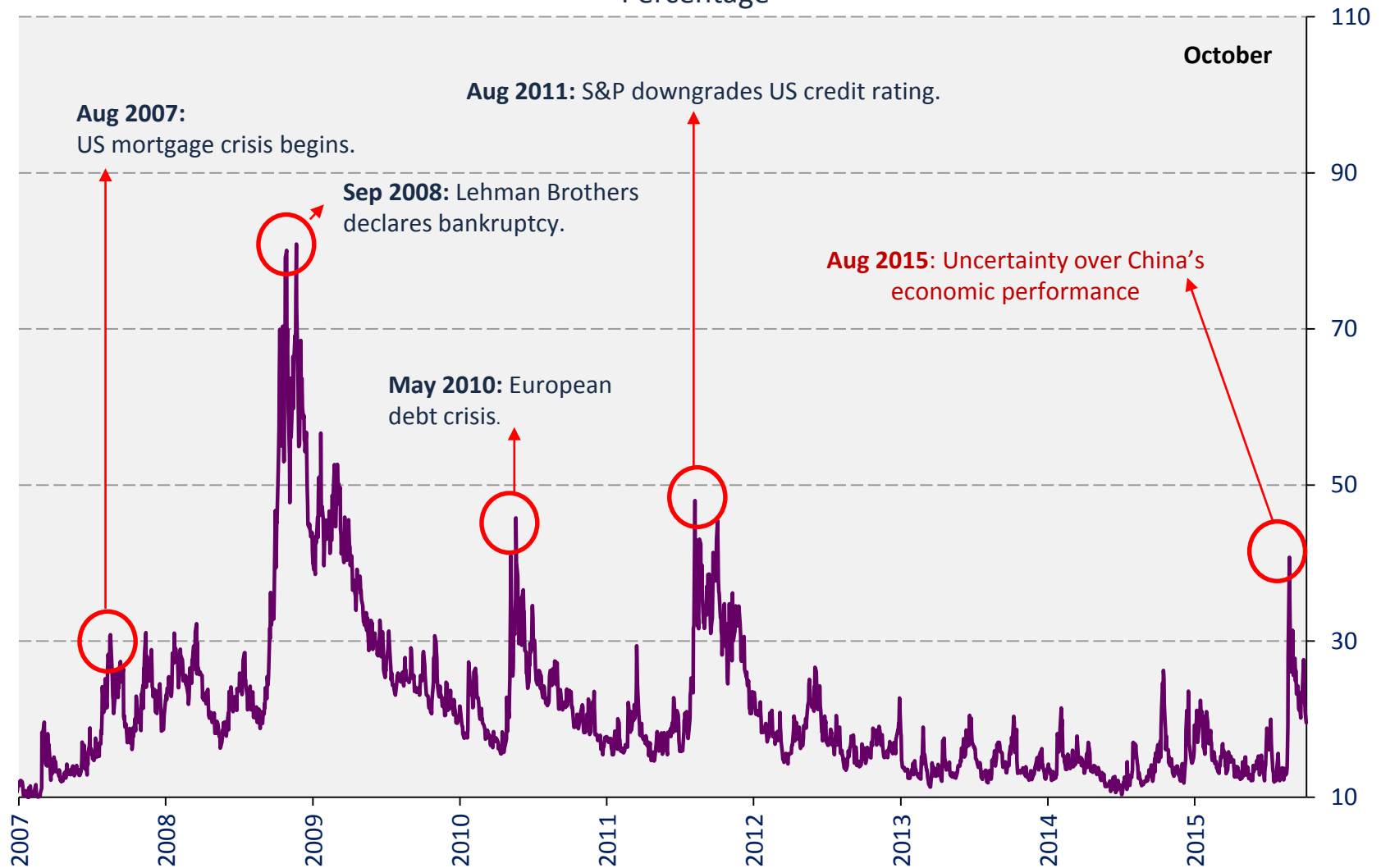
Source: Bloomberg.

1/ The CRB Index of Thomson Reuters is composed of 19 commodities, which are divided in 4 groups: energy (39%), agricultural (41%), precious metals (7%) and industrial metals (13%). Its subcomponent, CRB without energy, is composed of 15 commodities which are divided in 3 subgroups: agricultural (67%), precious metals (12%) and industrial metals (21%).

Source: Bloomberg.

Financial markets volatility has increased, mainly reflecting the uncertainty that prevails about the timing and pace of future increases in the FED's policy rate.

**Evolution of the Implicit Volatility Index of the S&P500 (VIX)^{1/}
Percentage**

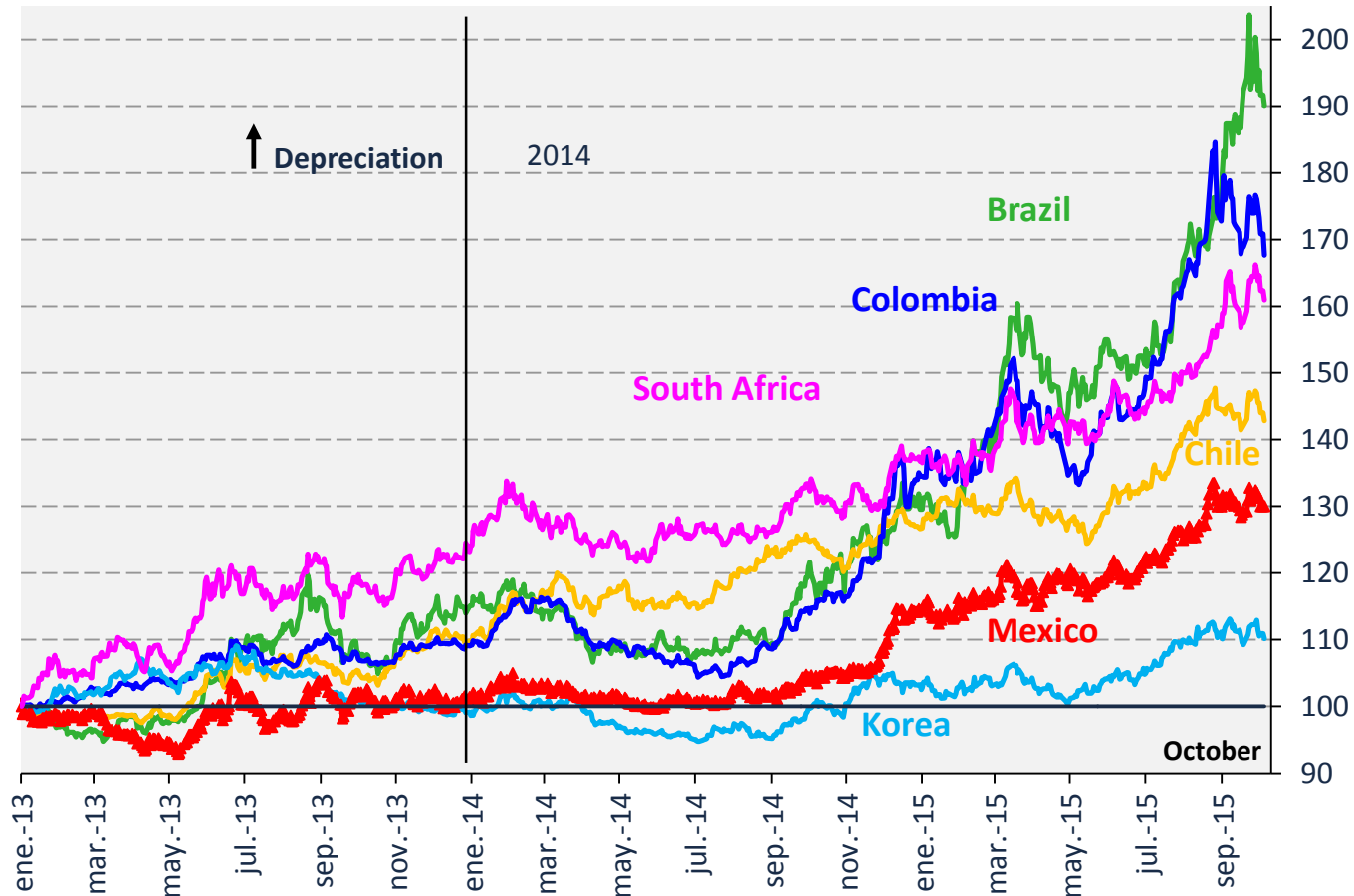


Source: Bloomberg.

^{1/} Refers to the weighted implicit-one-month-options volatility index for the S&P 500 published by the Chicago Board Options Exchange.

In this environment, emerging markets' currencies have depreciated significantly.

Emerging Economies: Nominal Exchange Rate
against USD
Index 01-Jan-2013 = 100



Source: Bloomberg.

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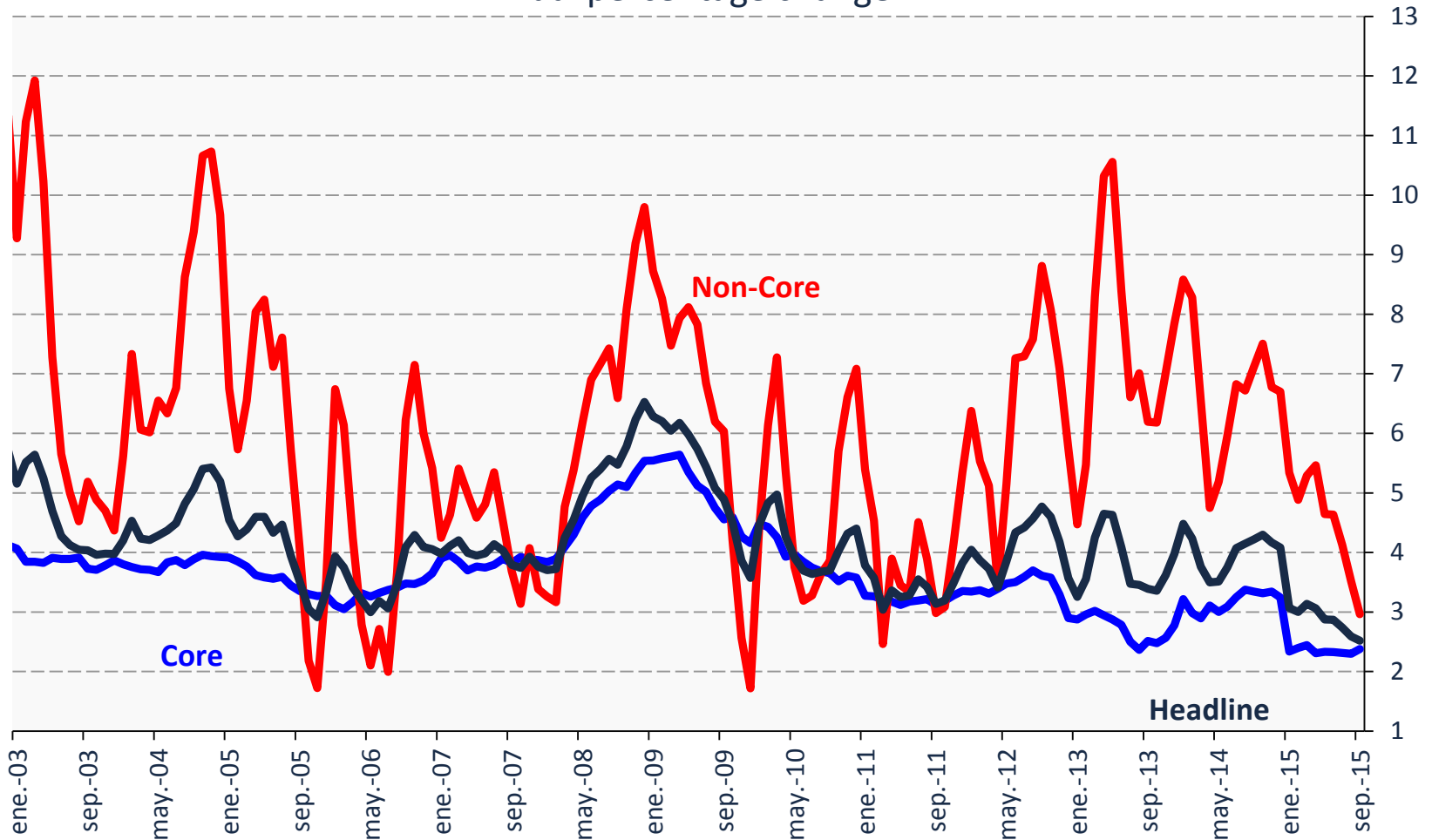
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Outlook and challenges

Inflation in Mexico is at minimum historical levels. The currency depreciation has not visibly impacted it.

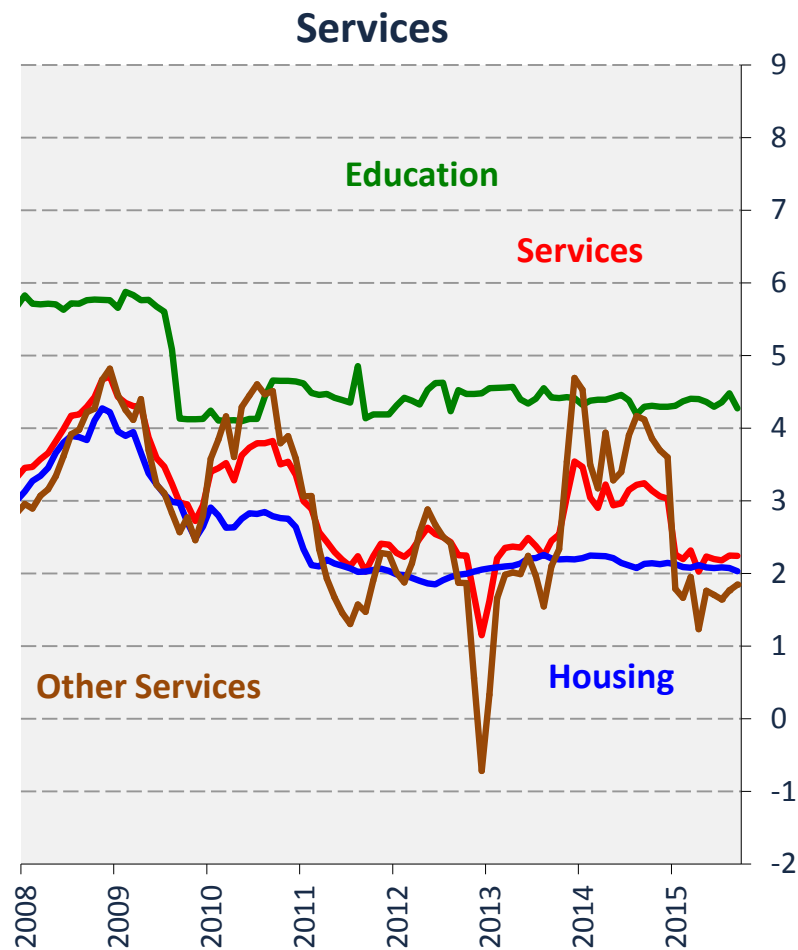
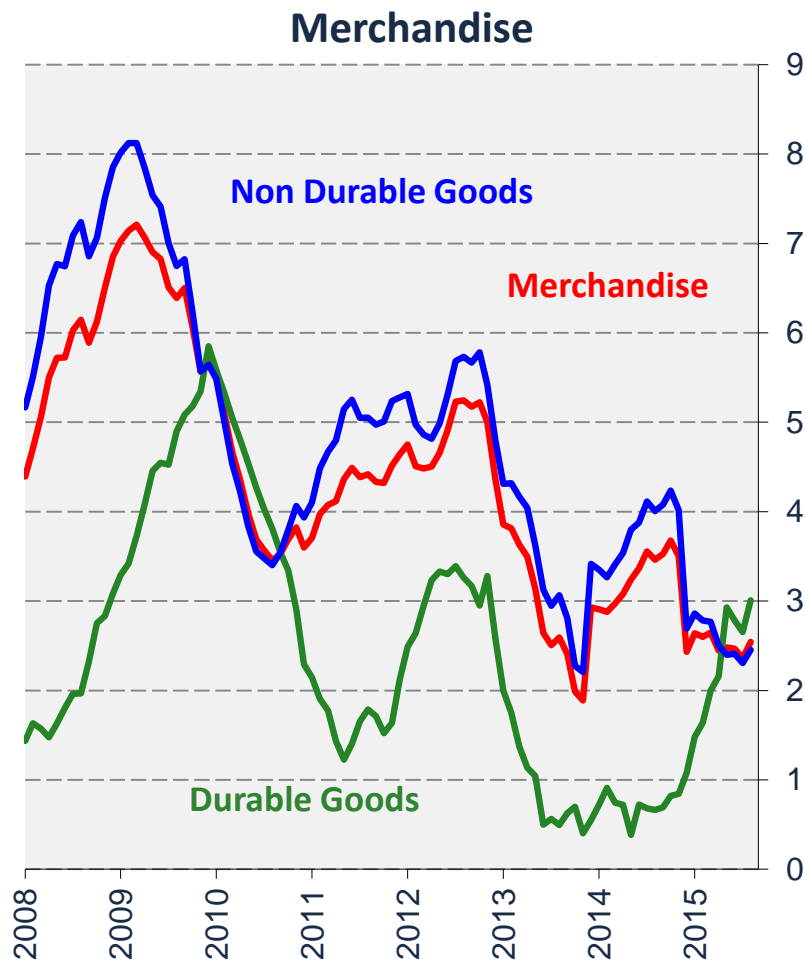
Consumer Price Index
Annual percentage change



Source: Banco de México and INEGI.
*/ Information up to september 2015.

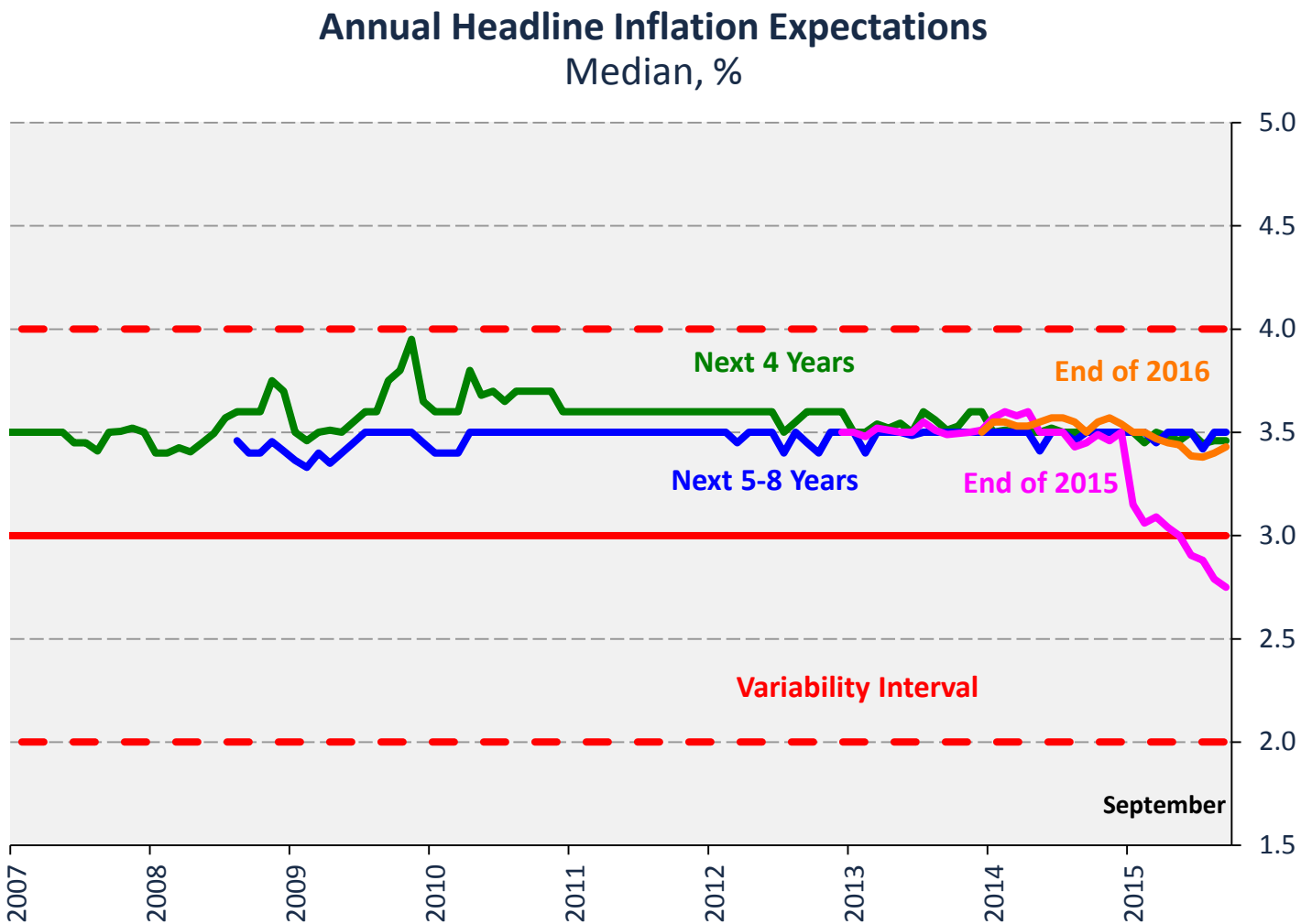
There seems to be some pass-through from the exchange rate to prices of durable goods, although there is no evidence of transmission to other prices in the economy.

Core Price Index
Annual percentage change



Source: Banco de México and INEGI.
*/ Information up to september 2015.

Inflation expectations remain well anchored.



Source: Banco de México Survey.

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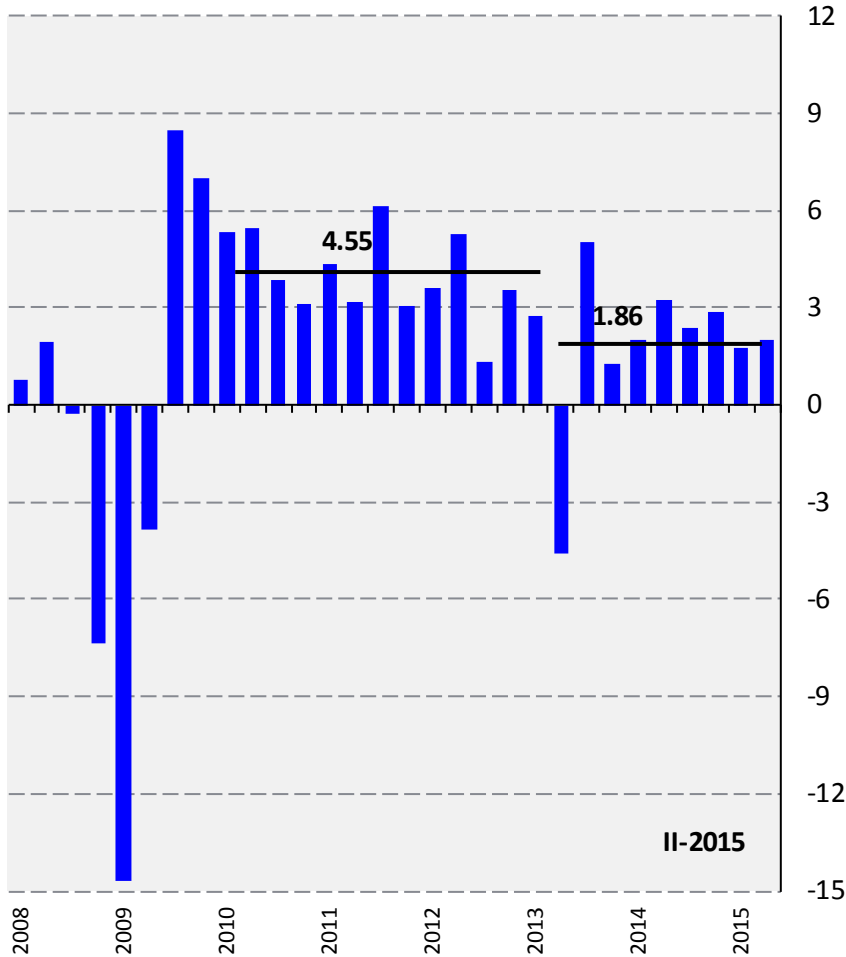
IV

Outlook and challenges

The Mexican economy has continued to grow at a moderate pace.

Gross Domestic Product

Annualized quarterly % change, s.a.

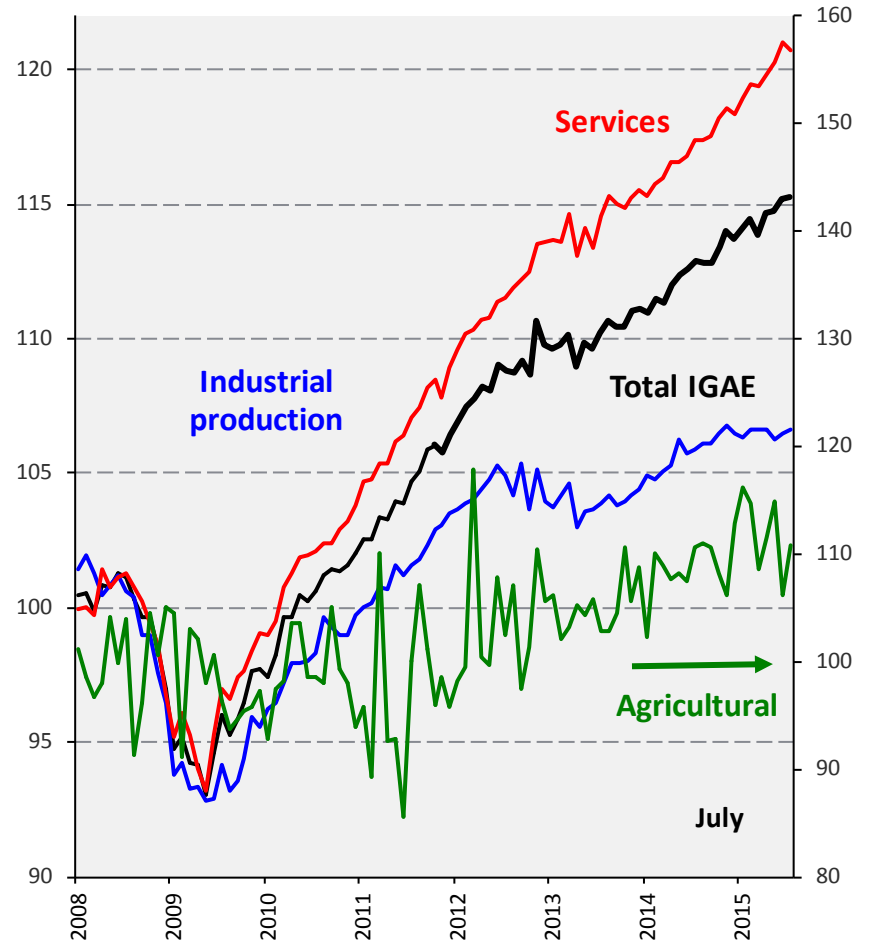


s. a. / Seasonally adjusted data.

Source: Mexico's System of National Accounts, INEGI.

Economic Activity Indicators

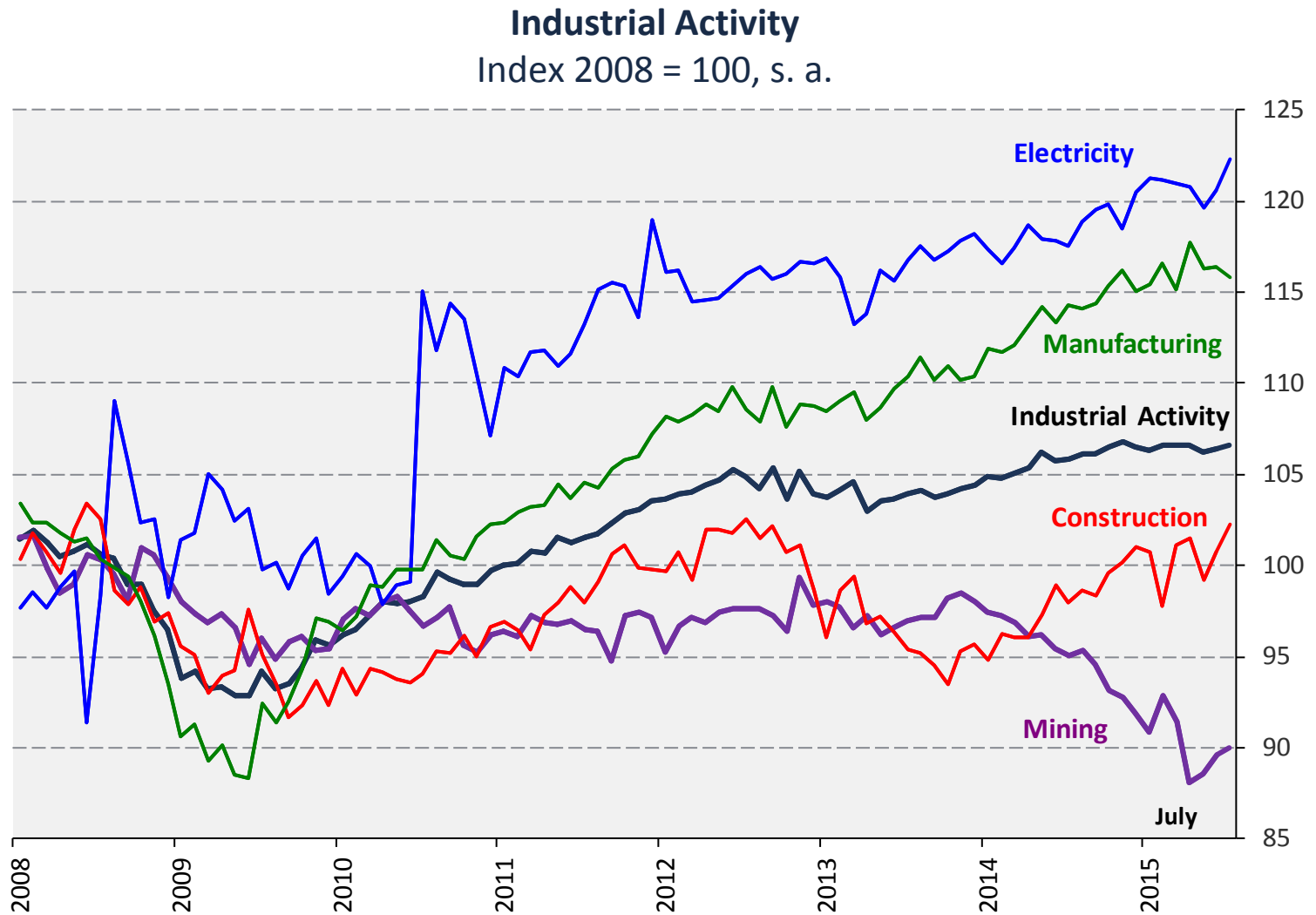
Index 2008 = 100, s. a.



s. a. / Seasonally adjusted data.

Source: Mexico's System of National Accounts, INEGI.

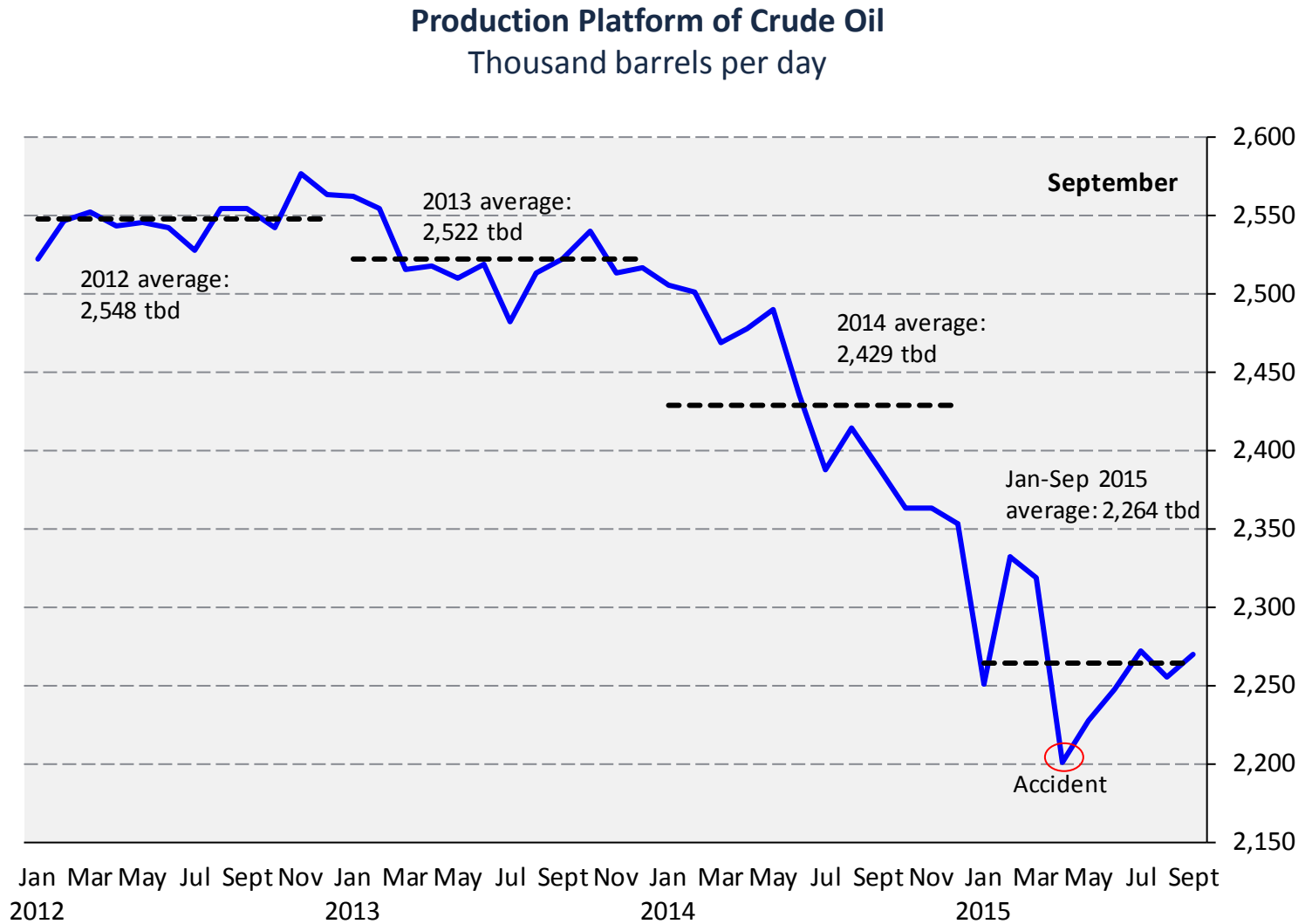
While manufacturing shows a positive growth trend, mining has been a drag for industrial activity and construction has remained subdued.



s. a. / Seasonally adjusted data.

Source: Mexico's System of National Accounts, INEGI.

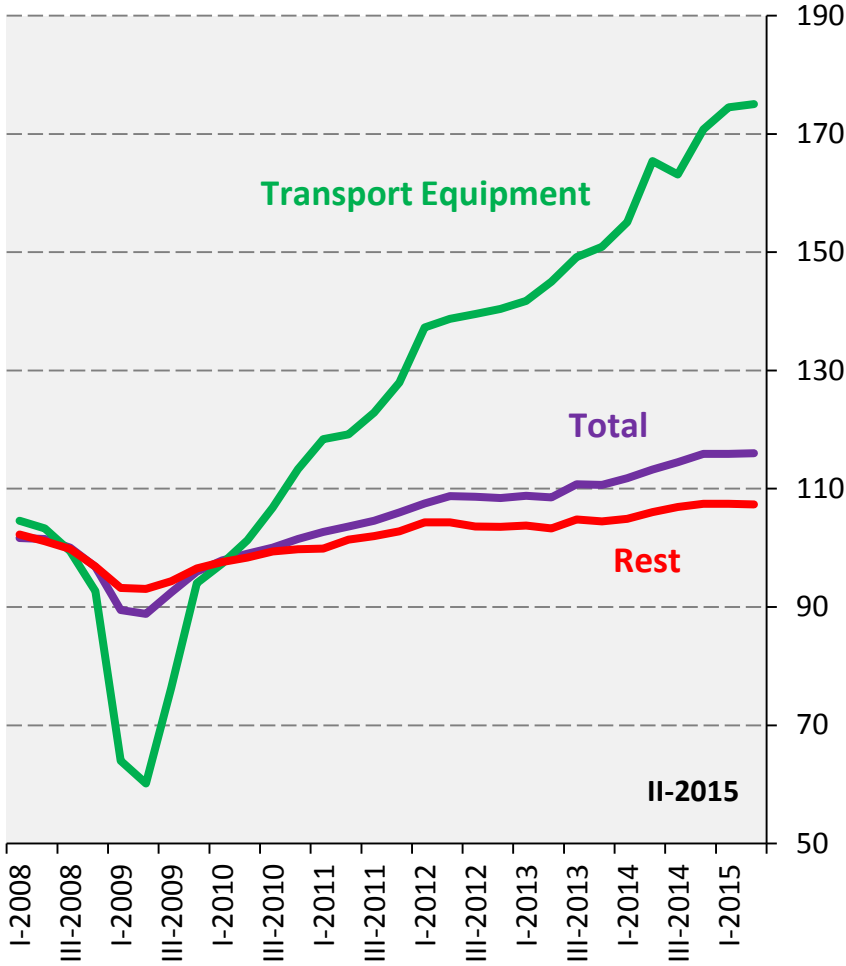
Production of crude oil has experienced an important reduction.



Source: Pemex.

Transport equipment production remains the main driver of manufacturing.

Manufacturing GDP
Index 2008 = 100, s.a.



Source: INEGI.

Production of Light Vehicles
Thousand units, s.a. annualized



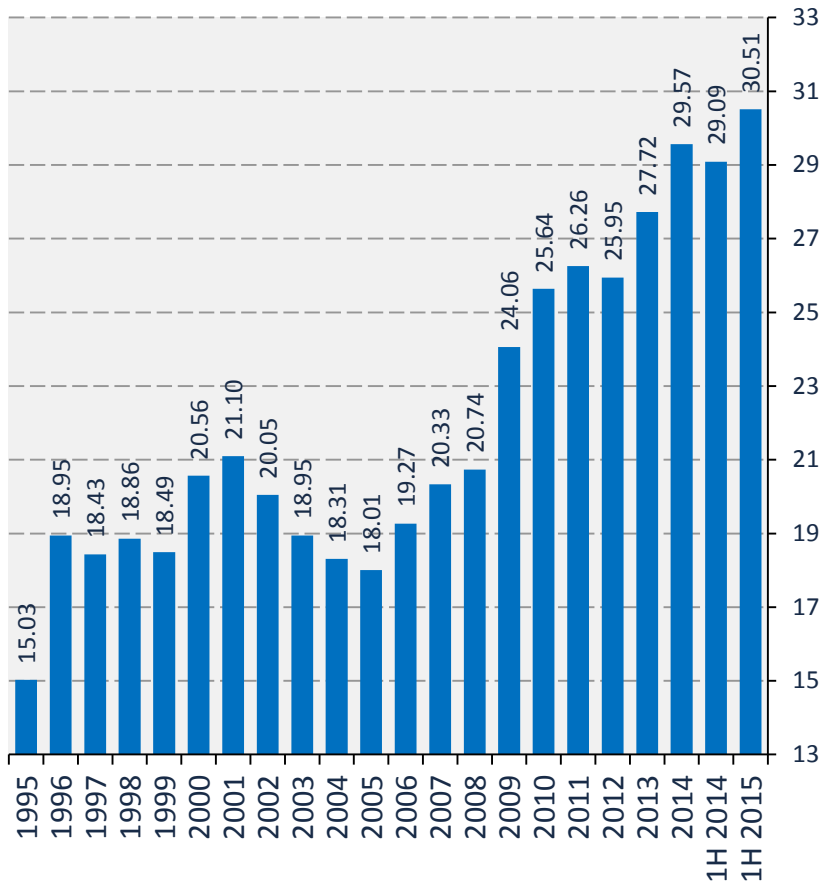
s. a. / Seasonally adjusted data.

Source: Banco de México with information from AMIA.

The performance of the automotive industry has been strong in recent years and is posed to continue that way.

Share of Imports from Mexico in total U.S. Automotive Imports

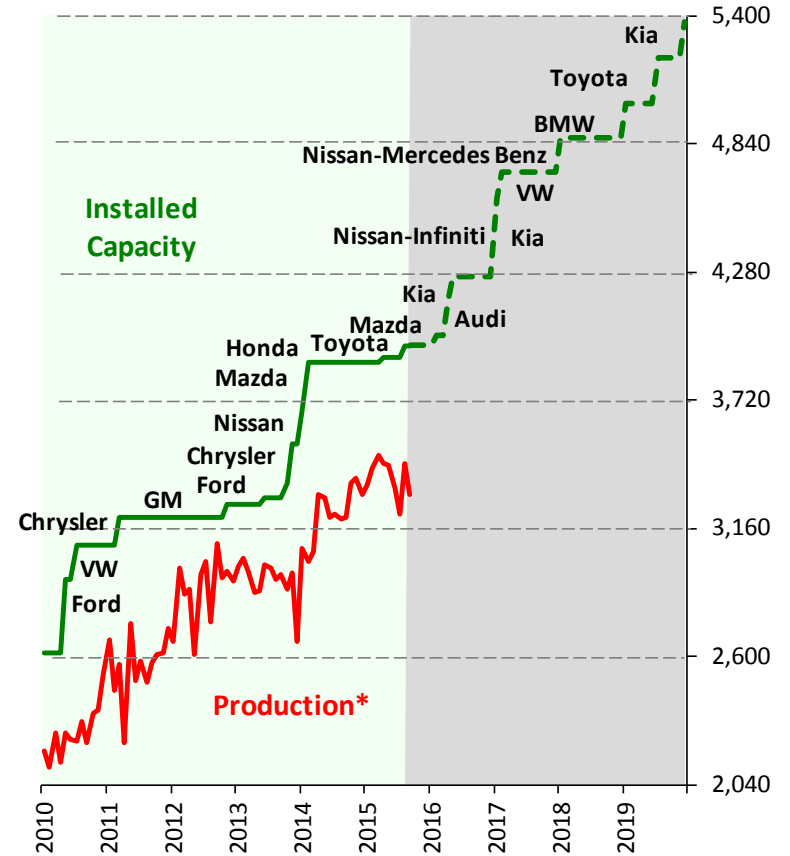
%



Source: Prepared by Banco de Mexico with data from U.S. Census Bureau.

Light Vehicles Production and Installed Capacity

Thousands units, s.a. annualized

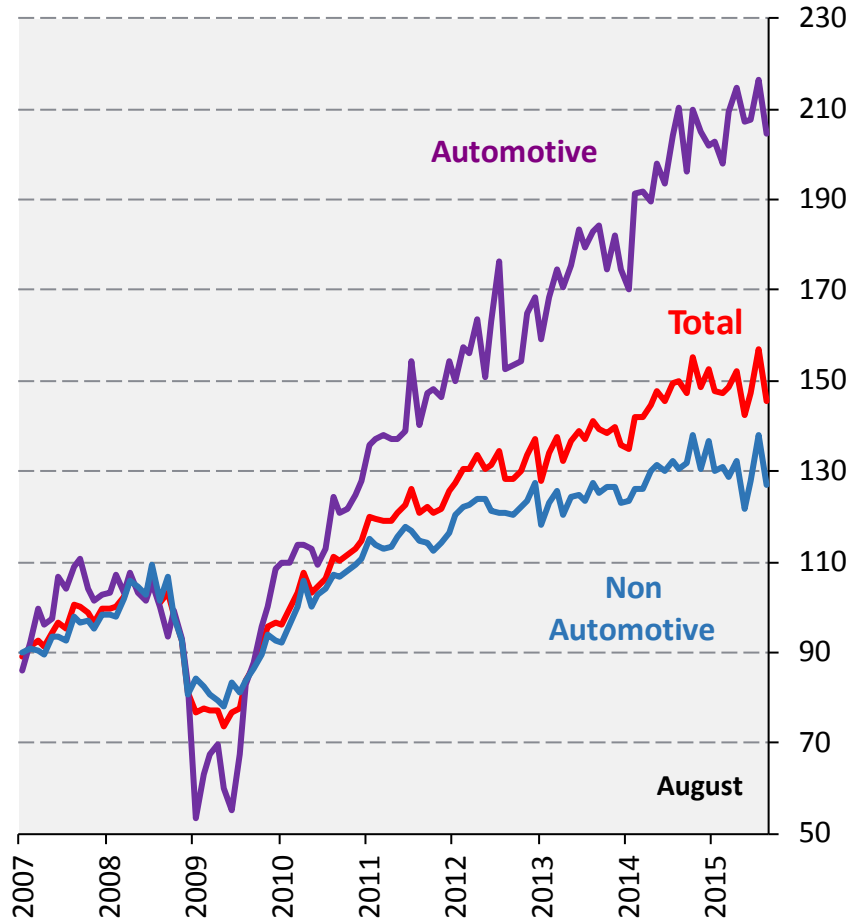


s. a. / Seasonally adjusted data for production.

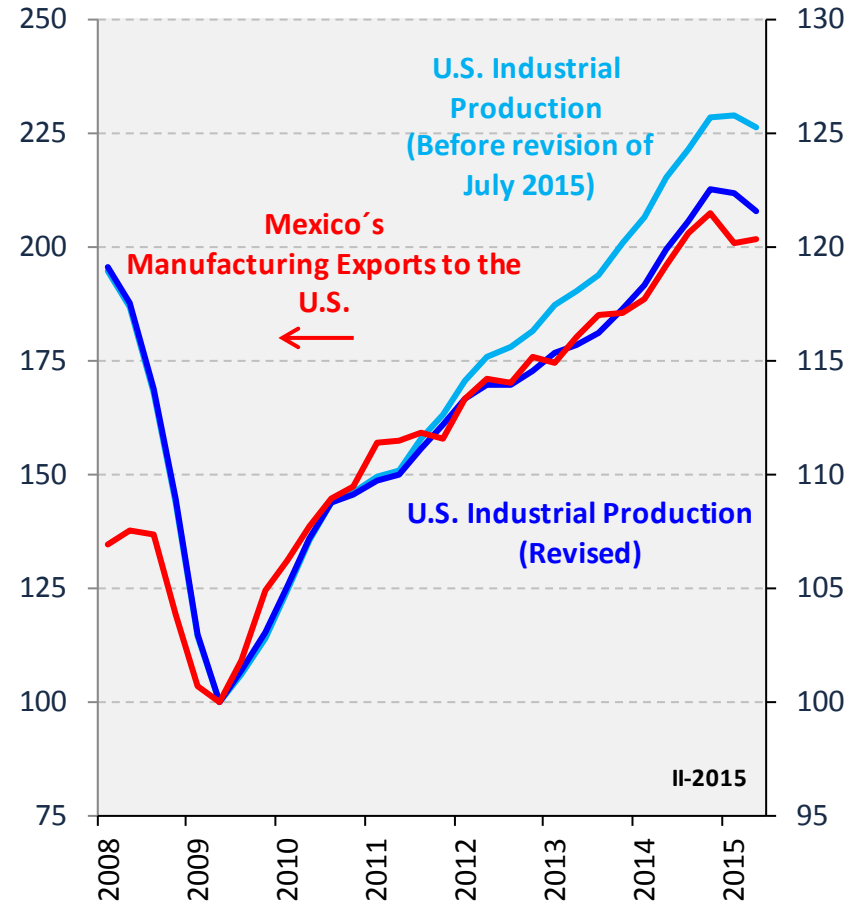
Source: Production data elaborated and seasonally adjusted by Banco de México with information from AMIA. Installed Capacity estimation based on press releases of assemblers and news.

Exports lost some dynamism mainly because of weak performance of manufacturing in the U.S., given that manufacturing exports from Mexico are still tightly linked to U.S. industrial production.

Manufacturing Exports
Index 2008 = 100, s.a.



U.S. Industrial Production and Mexico's Manufacturing Exports to the U.S.
Index 2009-II=100, s. a.



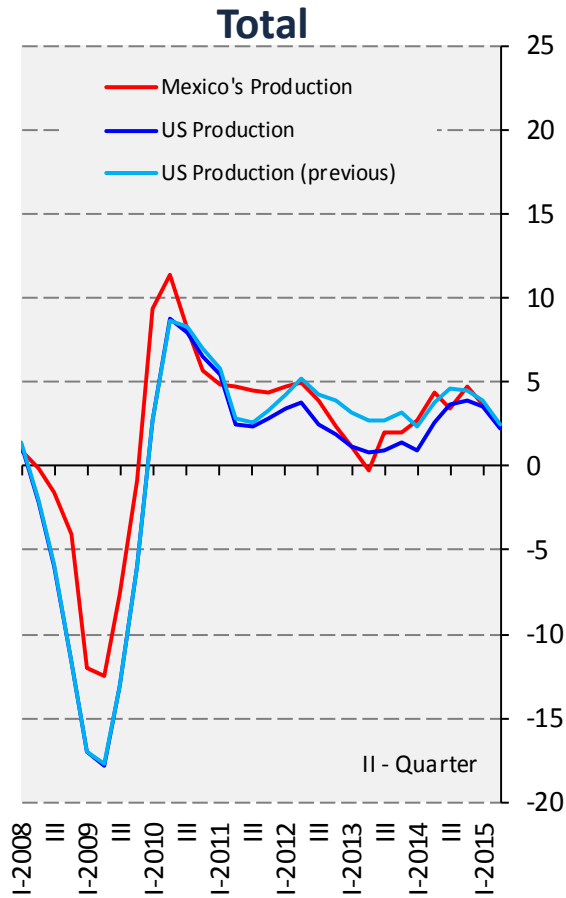
s.a. / Seasonally adjusted data.

Source: Federal Reserve Board and Banco de Mexico with information from SAT, SE, INEGI, *Balanza Comercial de 16 Mercancías de México* and SNIEG.

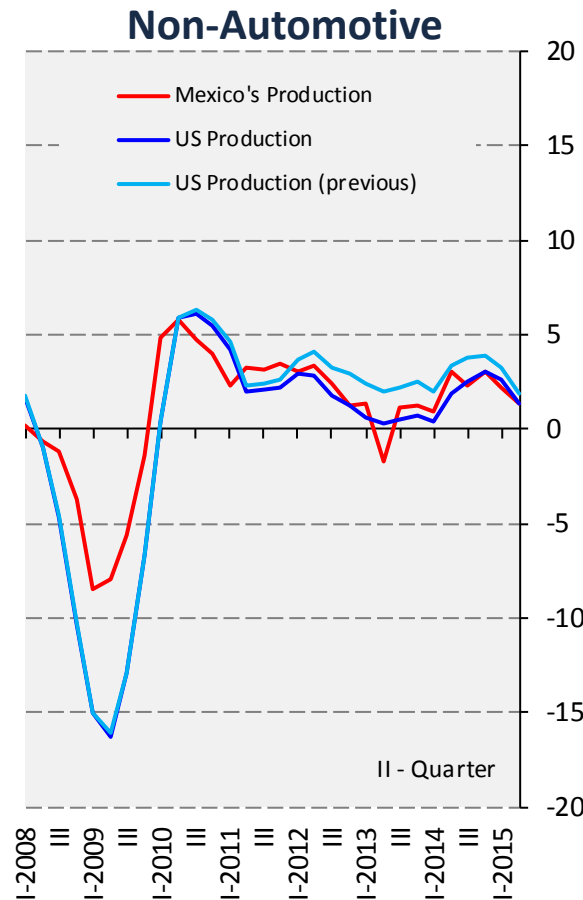
Source: SAT, SE, Banco de México, INEGI, *Balanza Comercial de Mercancías de México* and SNIEG.

Indeed, there is a high correlation between U.S. and Mexico's manufacturing sectors.

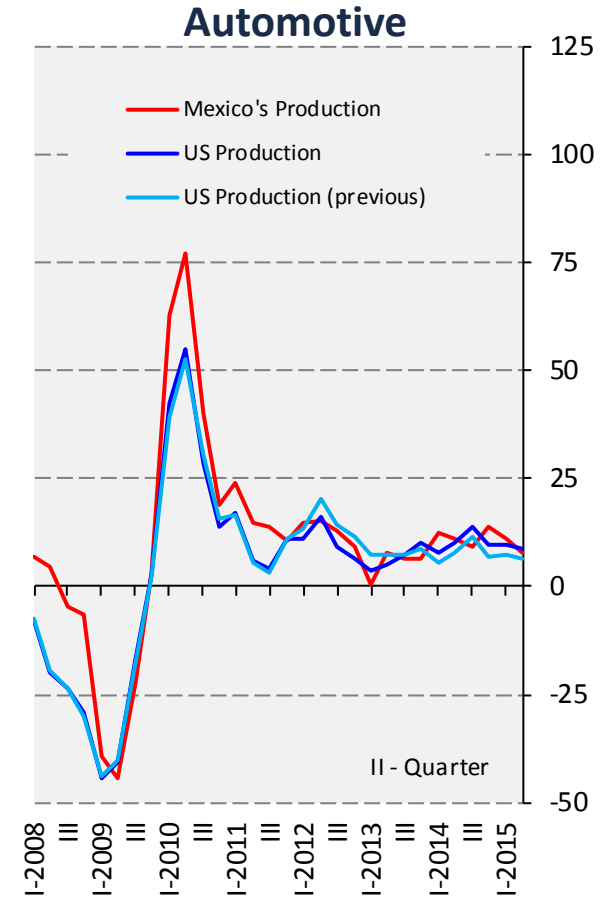
Manufacturing Production of the U.S. and Mexico Annual percentage change, s.a.



s. a./Seasonally adjusted data.
 Source: INEGI and Federal Reserve Board.



s. a./Seasonally adjusted data.
 Source: INEGI and Federal Reserve Board.

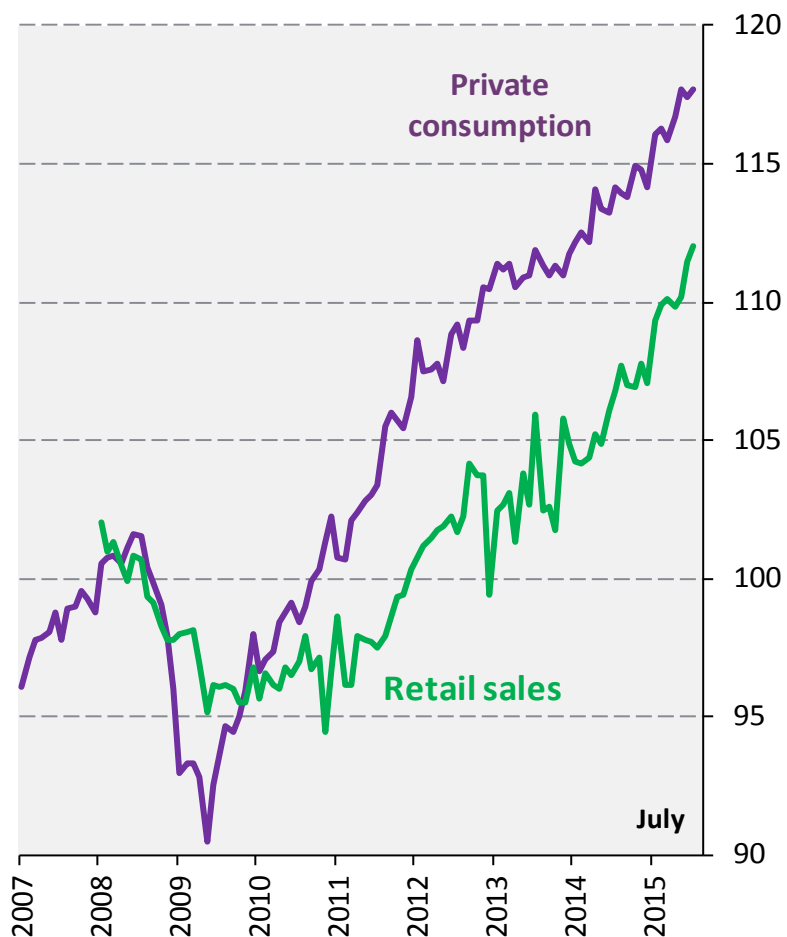


s. a./Seasonally adjusted data.
 Source: INEGI and Federal Reserve Board.

Consumption and investment are growing at a steady pace.

Monthly Indicator of Private Consumption in the Domestic Market and Retail Sales

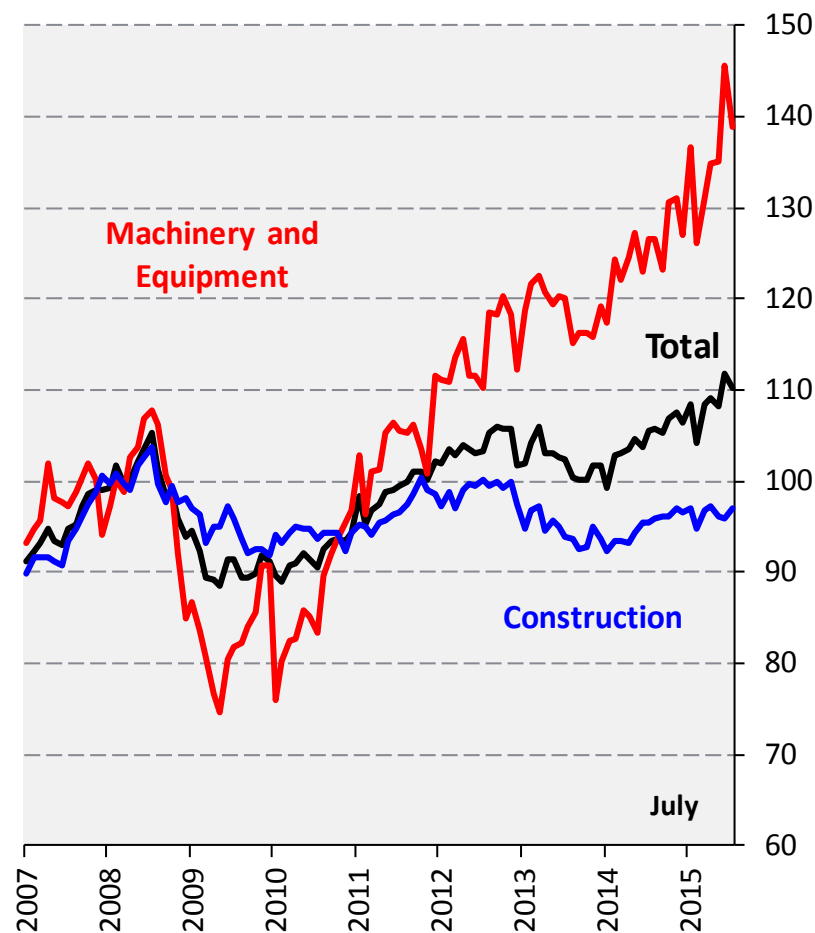
Index 2008=100, s. a.



s. a. / Seasonally adjusted data.
Source: INEGI.

Investment and its Components

Index 2008=100, s. a.



s. a. / Seasonally adjusted data.
Source: Mexico's System of National Accounts, INEGI.

The labor market still shows some slack.

National Unemployment Rate

% of LFP, s. a.

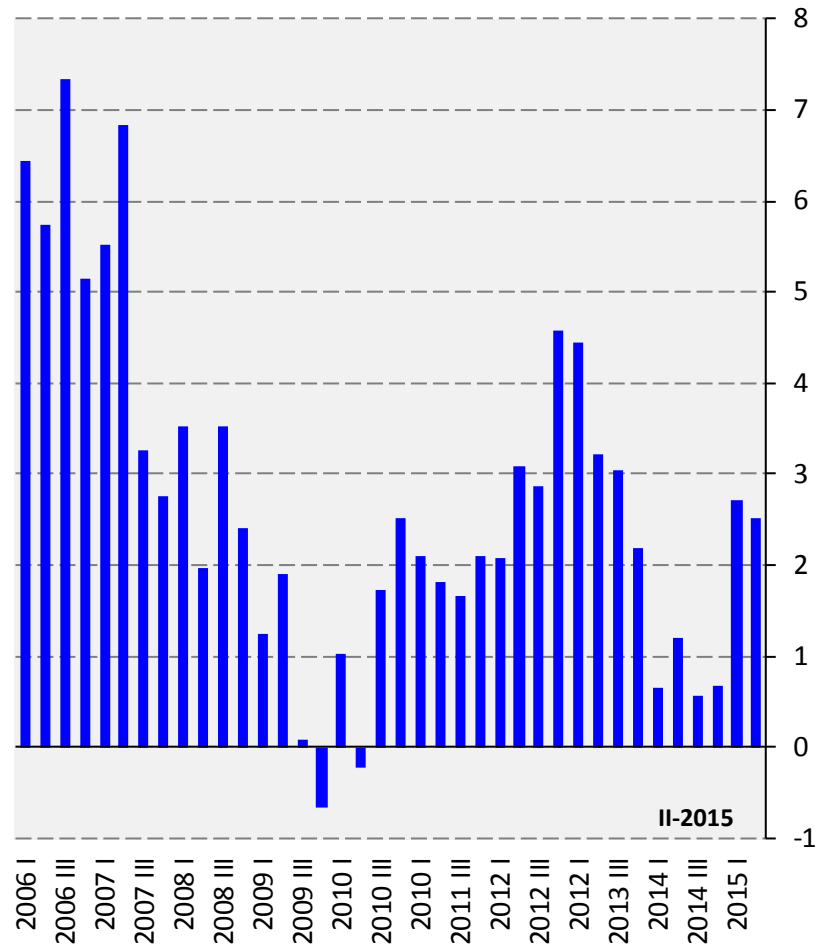


LFP/ Labor Force Participation.
s. a. / Seasonally adjusted data.

Source: National Employment Survey (*Encuesta Nacional de Ocupación y Empleo*), INEGI.

Average Nominal Wage of Salaried Workers

Annual percentage change



Note: Top and bottom 1% percentiles not included in the nominal wage calculation, neither workers with zero income or not reporting wage not are included.

Source: National Employment Survey (*Encuesta Nacional de Ocupación y Empleo*), INEGI.

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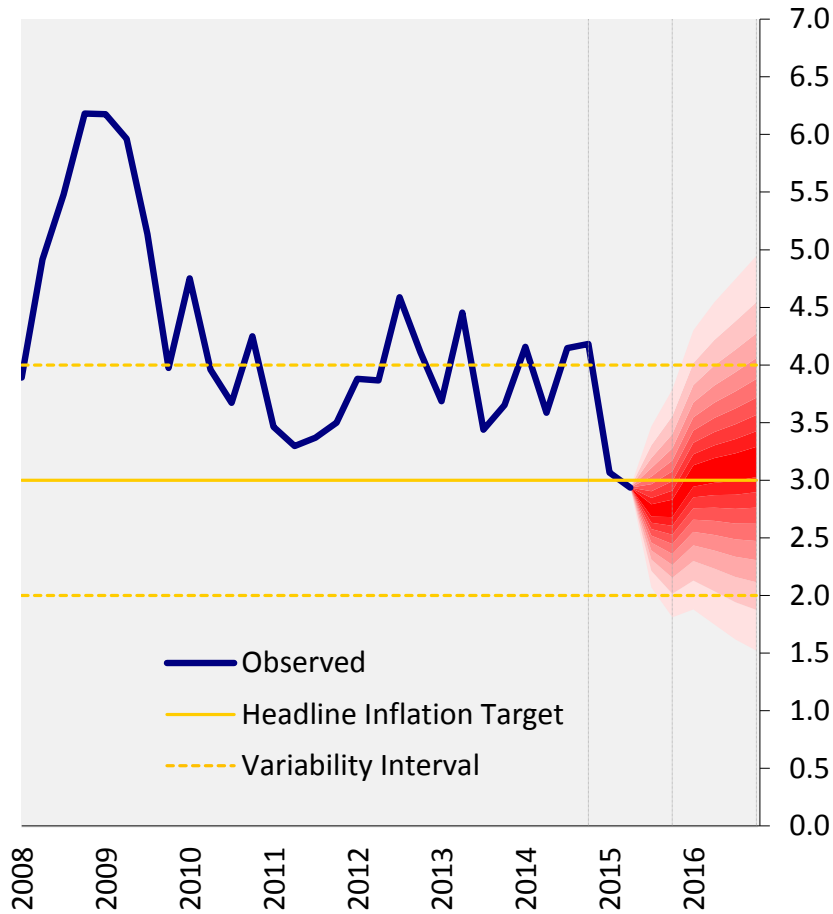
Economic Activity

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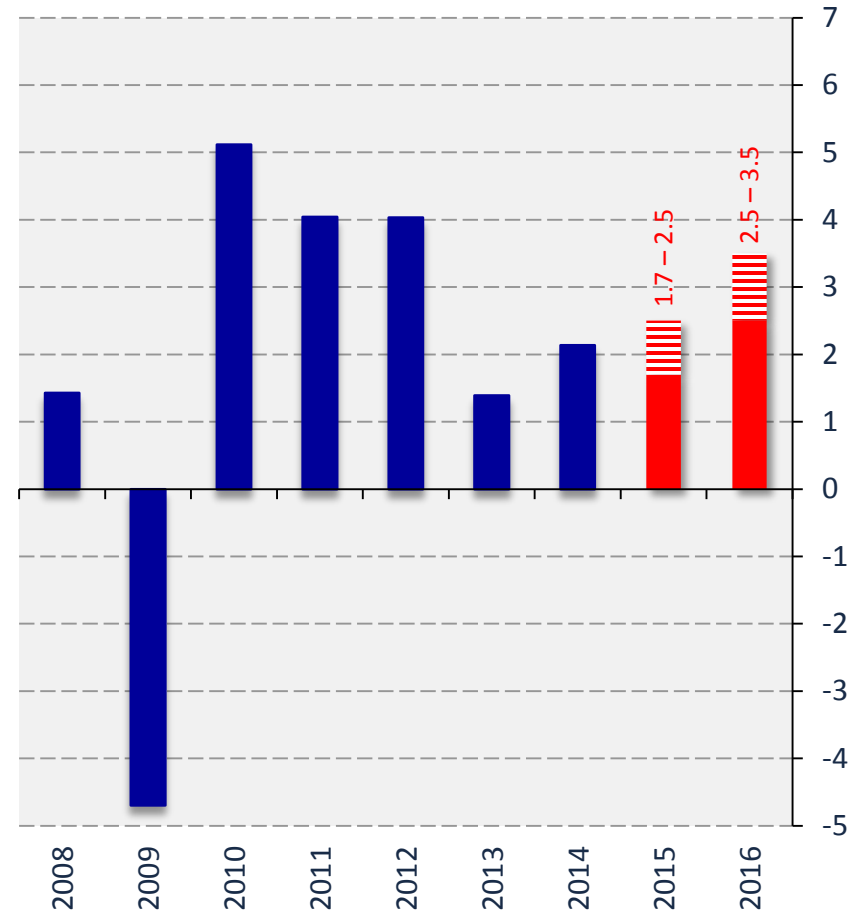
Outlook and challenges

Outlook for the Mexican economy.

Annual Headline Inflation ^{1/}
%



Gross Domestic Product
Annual % change, s.a.



s. a. / Seasonally adjusted data
 1/ Quarterly average of annual headline inflation.
 Source: Quarterly Report April - June 2015, Banco de México

s. a. / Seasonally adjusted data
 Source: INEGI and Quarterly Report April - June 2015, Banco de México

Risks to the Growth Outlook:

Upward:

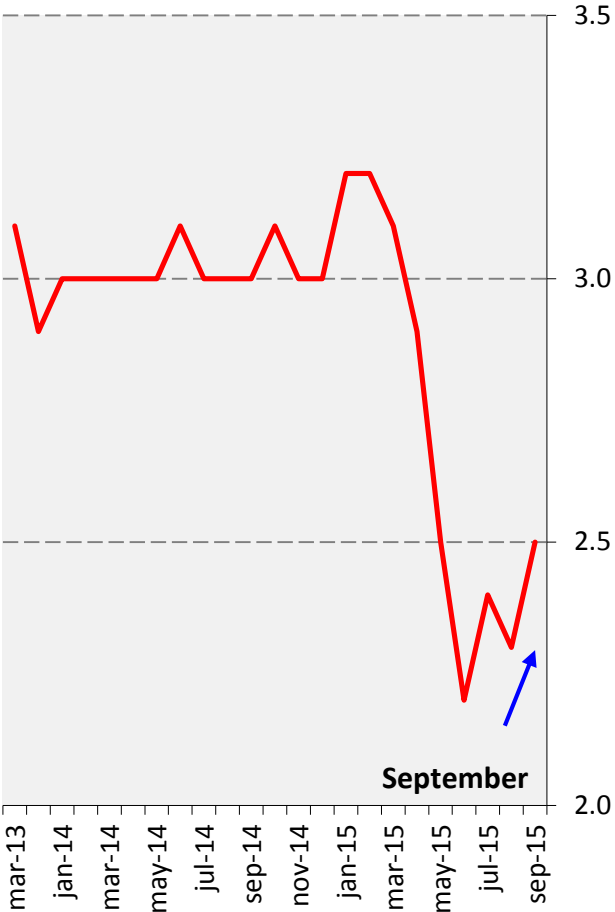
- ✓ A greater dynamism of the **exports'** sector, given a greater than expected recovery of external demand and a real exchange rate depreciation.
- ✓ Rapid progress in the implementation of **structural reforms** and in the strengthening of the rule of law.

Downward:

- ✓ That **manufacturing exports** keep registering a low dynamism, if the U.S. industrial sector maintains a weak performance.
- ✓ A deterioration in **investors' outlook**.
- ✓ A delay in the recovery of the national **oil production** in Mexico.
- ✓ A further increase in international financial markets **volatility**.

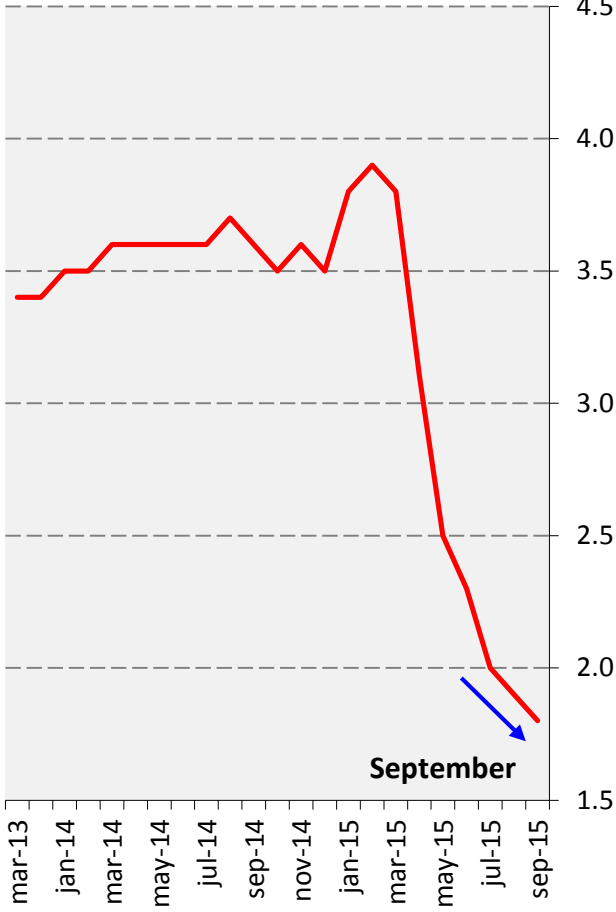
U.S. Economic Forecast.

2015 US GDP Forecasts
Annual percentage change



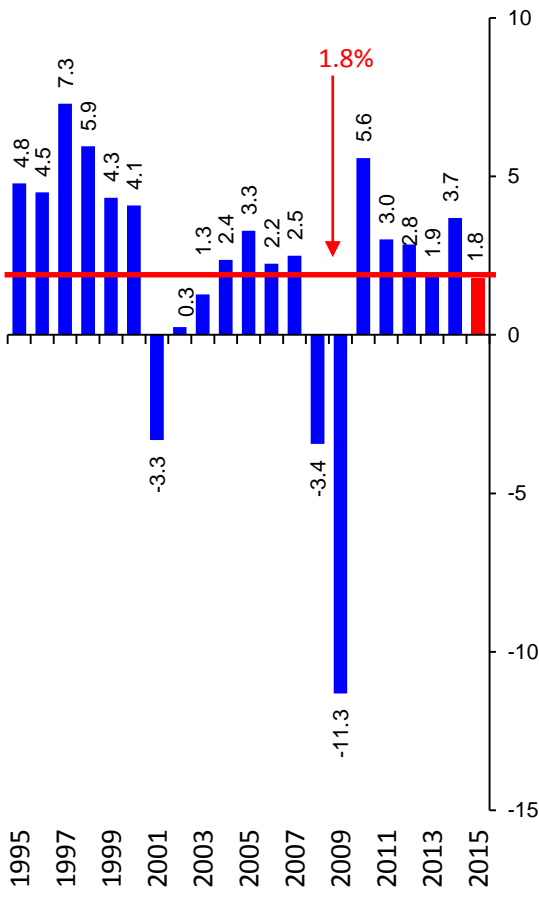
Source: Blue Chip.

2015 US IPIUS Forecasts
Annual percentage change



Source: Blue Chip.

US Industrial Production Index
Annual percentage change, s.a.



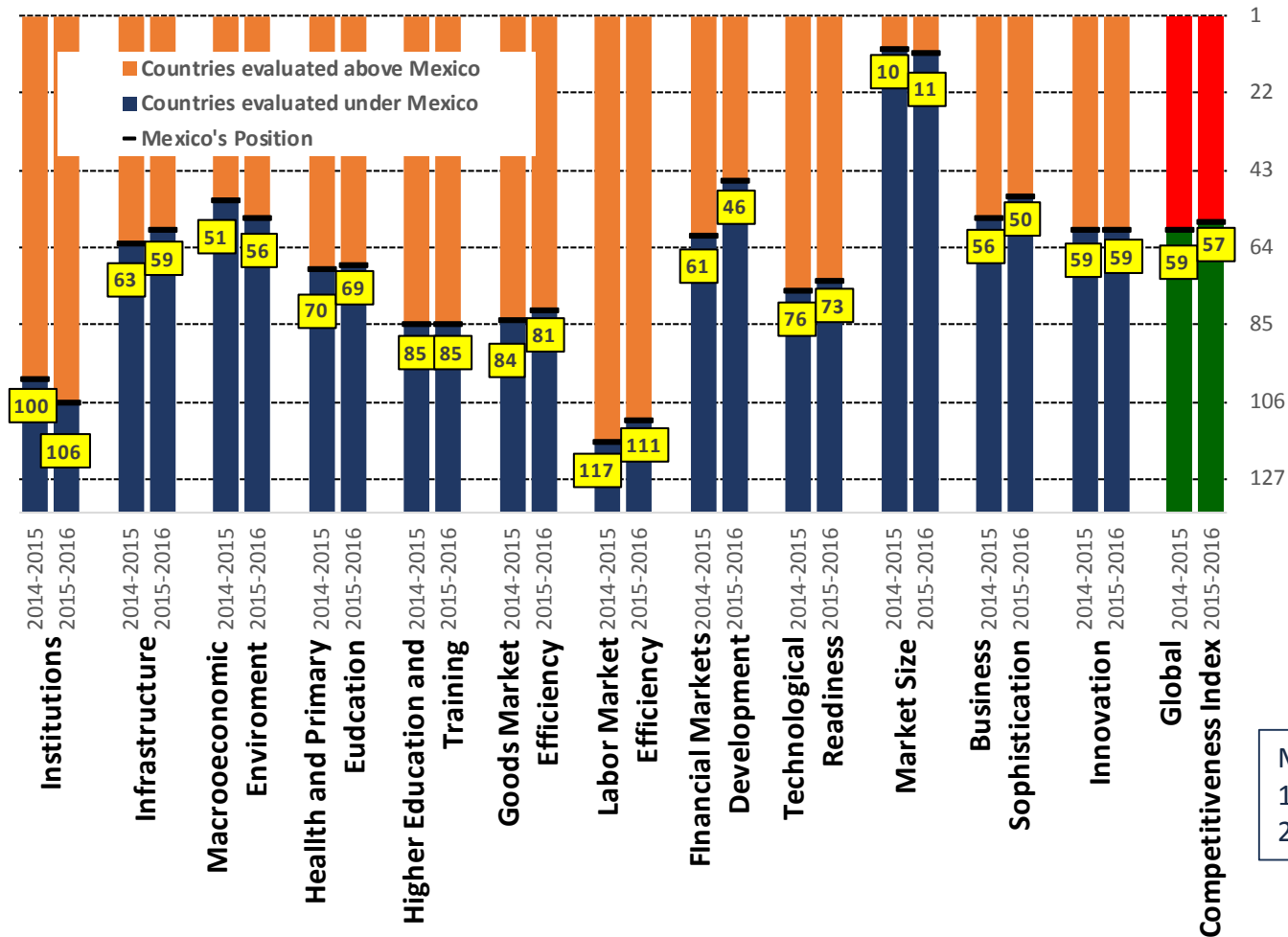
s. a. / Seasonally adjusted data.
Source: Federal Reserve Board and Blue Chip.

Challenges for the Mexican Economy

- ① Given the complex international environment, it is key to preserve a **solid macroeconomic framework**.
- ② The strength of institutions is crucial to back a good functioning of the economy. For this reason Mexico should make an additional effort to strengthen **the institutions** and **the rule of law**.
- ③ In order to achieve **higher and sustainable growth rates**, it is necessary to increase investment and productivity, which, in turn, requires clear progress in the implementation of structural reforms. Recent developments, like the auctions of oil fields and changes in telecommunications prices and retail conditions, suggest such implementation is starting to bear fruit.

Global Competitiveness Index 2015-2016

Mexico's Relative Position in each of the 12 competitiveness pillars and in the Global Index
 Sample of countries evaluated in both the previous and current reports



Mexico's Ranking*
 1) 2014-2015: 61
 2) 2015-2016: 57

* Position in the ranking using the whole sample for each report.

Ranking goes from 1 up to 136 according to the set of countries that compose the constant sample index.

Source: Global Competitiveness Report 2014-2015 and 2015-2016, World Economic Forum.

The timely and adequate implementation of growth enhancing reforms is crucial to achieve high and sustainable economic growth rates.

- 1 Labor
- 2 Education
- 3 Competition
- 4 Telecommunication
- 5 Energy
- 6 Financial
- 7 Transparency
- 8 Anti- corruption

