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The Peso Devaluation's Impact on Texas

"Texas' economy should continue to expand in 1995, but the peso devaluation will slow the state's growth."

Texas' close economic ties with Mexico will make the impact of the peso's plunge much stronger here than in other parts of the United States.

In the six weeks between December 20, 1994, and February 1, 1995, the Mexican peso lost roughly 40 percent of its value. This dramatic devaluation should have few long-term effects on the level of U.S. employment, but it could have a substantial influence on the kinds of jobs people do and where they do them. Nowhere will these shifts be more evident than in Texas.

Texas Effects

The short-term impact of the peso devaluation could be four times stronger in Texas than in the rest of the United States. One-third of U.S. exports to Mexico come from Texas. As Texas' largest foreign trading partner, Mexico plays a greater role in the Texas economy than in the U.S. economy. Excluding trade with Mexican maquiladora plants, Mexico receives 27 percent of Texas' merchandise exports, compared with 6 percent of U.S. merchandise exports.[1] Exports to Mexico represent nearly 2 percent of Texas output but less than 0.5 percent of U.S. output.

A 40-percent devaluation and its multiplier effects could cost approximately 1 percent of the state's total employment, or about 75,000 jobs, over the next three years. Because the state has been gaining employment at an annual rate of 240,000 jobs per year, such a loss represents about four month's worth of growth.

Texas' economy should continue to expand in 1995, but the peso devaluation will slow the state's growth. Before the devaluation, Texas employment was predicted to grow around 2.8 percent in 1995. With a 40-percent devaluation of the peso, growth near 2.5 percent is more likely.

As the effects of the peso devaluation ripple through the Texas economy, some industries will feel a much greater impact than others. The devaluation makes Texas exports —sold in dollars—more expensive in pesos and Mexican imports—sold in pesos—relatively cheaper in dollars.

In the near term, Mexico's demand for Texas goods and services may drop, which will mean production cutbacks for Texas industries that are sensitive to peso–dollar exchange rate fluctuations.

Other Texas firms may lose business to Mexican imports, while Texas industries that import goods and services from Mexico will benefit from relatively cheaper prices of Mexican products.

Along the U.S.–Mexico border, businesses are seeing less cross-border shopping and tourism because of the peso's loss of buying power. The devaluation's effect on retailing, health care, tourism and other service industries is difficult to quantify because statisticians do not measure international trade in services at the state level. Figures on merchandise exports, however, can help predict how the devaluation will affect specific manufacturing industries in Texas.

Peso-Sensitive Industries

Furniture manufacturers, car makers and electronics firms will be the Texas industries hardest hit by the devaluation, according to a Federal Reserve Bank of Dallas index that measures the sensitivity of manufacturing industries to devaluations of the peso.[2] Table 1 ranks Texas manufacturing industries according to their peso-sensitivity and shows the dollar volume of their exports to Mexico. The table reflects trade and production patterns for 1993. Because of their special import–export status, maquiladora products are excluded.

Texas furniture and fixtures manufacturing is the state's most peso-sensitive industry because two-thirds of its total sales to foreign countries go to Mexico. Roughly 30 percent of Texas' exports of electronics and transportation equipment goes to Mexico.

Among the less-sensitive manufacturing categories are industrial machinery (including computer equipment), petroleum and coal products, textile mill products, and printing and publishing. Firms in these industries send a relatively small share of their total exports to Mexico. For instance, once exports to maquiladoras are excluded, the Texas industrial machinery industry sends only 12 percent of its exports to Mexico.

Table 1
Texas Industries' Sensitivity to Changes in the Value of the Mexican peso

	Peso Sensitivity	Exports* (millions of dollars)
Furniture and fixtures	.988	$ 160.04
Transportation equipment	.922	965.11
Electronics and electric equipment	.811	1,543.58
Leather and leather products	.699	61.17
Apparel and other textile products	.628	156.02
Miscellaneous manufacturing industries	.610	134.70
Lumber and wood products	.609	134.28
Fabricated metal products	.504	319.16
Primary metal industries	.482	463.11
Stone, clay and glass products	.455	50.79
Rubber and miscellaneous plastics products	.413	283.75
Food and tobacco	.379	996.51
Paper and allied products	.351	454.75
Instruments and related products	.326	228.69
Chemicals and allied products	.228	665.38
Printing and publishing	.203	54.85
Industrial machinery (including computer equipment)	.173	934.31
Petroleum and coal products	.145	391.42
Textile mill products	.124	83.08
All manufacturing	.389	8,080.68

* These estimates of 1993 exports by industry exclude exports to Mexican maquiladora firms.

Conclusion

Some analysts who considered the peso to be overvalued before the devaluation now think Mexico's currency is undervalued. If so, then the peso should recover some of the ground it has lost over recent weeks. Any improvement in the value of the peso would reduce the magnitude of the devaluation's effects but not their distribution. Peso-sensitive industries and the border region would still bear the brunt of production cutbacks and job losses.

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Notes

[1] These estimates reflect an adjustment for exports to Mexican maquiladora plants. We exclude exports to maquiladoras from the export data because those goods are only exported to Mexico temporarily. Under a typical maquiladora's production-sharing agreement, goods enter Mexico duty-free and ultimately return to the United States duty-free (the United States charges a duty only on the non-U.S. content of the products). We also exclude the U.S. content of imports from maquiladoras from the import data that are used in the analysis.

In 1993, the most recent year for which we have complete information, U.S. exports to Mexico totaled $41.6 billion, of which the Mexican government considered $15.9 billion to be exports to maquiladoras. To derive Texas exports to maquiladoras, we assume that Texas exports to maquiladoras in each industry are proportional to U.S. exports to maquiladoras for that industry. Thus, if maquiladora exports represent 10 percent of U.S. exports in a given industry, we assume that maquiladora exports represent 10 percent of Texas exports in that industry.

[2] Lori L. Taylor developed this index, using work by W. Michael Cox and John K. Hill in "Effects of the Lower Dollar on U.S. Manufacturing: Industry and State Comparisons," Federal Reserve Bank of Dallas *Economic Review*, March 1988. A technical appendix detailing her modifications to the Cox–Hill analysis is available from the authors.