Mexico’s economy contracted less than previously estimated in second quarter 2016. Gross domestic product (GDP) fell at an annual rate of 0.7 percent in the second quarter, according to the second estimate released by Instituto Nacional de Estadística y Geografía (National Institute of Statistics and Geography). In addition, more recent data on exports, employment, industrial production and retail sales also show improvement. Inflation held steady in August, but the peso fell against the dollar in September. The consensus 2016 GDP growth forecast edged down from 2.3 percent in July to 2.2 percent in August.

Output Falls in Second Quarter

Mexico’s GDP contracted at a 0.7 percent annualized rate in the second quarter (previous estimate was −1.2 percent) after growing 2 percent in the first (Chart 1). This is the first quarterly decline in output since second quarter 2013. Service-related activities (including trade and transportation) grew 0.6 percent in the second quarter, while output from goods-producing industries (including manufacturing, construction and utilities) fell 5.9 percent. Agricultural output dipped 1.4 percent.

Exports Increase in July

Overall exports edged up 0.5 percent in July after rising 5.8 percent in June. The three-month moving averages of total and manufacturing exports continued to edge up after declining throughout last year (Chart 2). Oil exports turned around earlier this year after falling since 2012. Notwithstanding this year’s reversal, oil exports remain at low levels and were down 36 percent in the first seven months of 2016 compared with the same period a year ago.

Industrial Production Expands

Mexico’s industrial production (IP) increased 0.3 percent in July after growing 0.1 percent in June. U.S. IP also increased in July (0.6 percent) but then fell 0.5 percent in August. The three-month moving average in Mexico’s IP shows signs of improvement after stagnating earlier in the year (Chart 3). Total IP, which includes manufacturing, construction, oil and gas extraction, and utilities, has been growing slower than manufacturing IP since early 2014.

Retail Sales Continue Growing

Retail sales expanded 1 percent in June after growing 1.2 percent in May. June sales were up an impressive 9.1 percent year over year. The smoothed data (three-month moving average) clearly show the sharp acceleration in sales revenue in the first half of 2016 (Chart 4). Despite this, the consumer confidence measure worsened in July and August.

Job Growth Remains Strong

Formal-sector employment—jobs with government benefits and pensions—grew at an annualized rate of 5.9 percent in August and was up 3.8 percent year over year (Chart 5). Year-to-date job growth has been nearly the same as in 2015 when employment expanded 3.8 percent (December over December). This is above the 3.1 percent historical average pace of job gains.

Peso Loses Ground Against Dollar in September

The peso averaged 18.8 pesos per dollar in September, which is 2 percent lower than in August (Chart 6). The peso
has lost 11 percent of its value against the dollar on a year-over-year basis. The Mexican currency has been weak as a result of the anticipation of further increases in U.S. interest rates, as well as market turmoil resulting from low oil prices, weaker-than-expected global demand and Brexit.

**Inflation Holds Steady in August**

Inflation was 2.7 percent in August, the same as in July, and still slightly below the central bank’s long-term inflation target of 3 percent (Chart 7). Prices excluding food and energy rose 3 percent over the last 12 months. Mexico’s central bank raised its benchmark interest rate by 50 basis points to 4.25 percent in June following the UK’s vote to leave the European Union. This tightening followed on the heels of two earlier interest rate hikes in December 2015 and February 2016. Agustin Carstens, Mexico’s central bank governor, has made it clear that the central bank will not hesitate to use interest rate increases and currency interventions as needed to strengthen the peso and stabilize prices.

—Jesus Cañas

**About the Author**

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