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Mexico Consensus Economic Forecast

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CONSENSUS ECONOMIC FORECAST

MÉXICO

University of Texas at El Paso
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1st Quarter 2010

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A Much Better Year

The bounce back from last year's 6.5 percent plunge will give the Mexican economy a 2010 growth rate that is quite robust by historical standards. This year's projected growth rate of 3.6 percent will be slightly higher than the 3.4 percent average annual growth rate between 2000 and 2009.

Fuelled by higher taxes and public sector prices, modest recovery of demand, and the pricing power of dominant players in key sectors of the Mexican economy, inflation will rise this year to 5.2 percent, its fourth highest level of the decade. Even so, it will be minimal by the standards of the 1980's and 1990's, when inflation averaged 69.7 percent and 20.3 percent, respectively, on an annual basis.

The one-month *CETES* rate will average 4.66 percent this year, a historical low. In September, Banco de Mexico is expected to start raising the Mexican reference rate. Much like the Fed, *Banxico* is relying on the output gap to restrain inflation. However, they will also rely on the inflationary impact of government-mandated prices increases and higher taxes to run their course this year.

The balance of payments should not present any reason for the peso to devalue. Direct foreign investment (DFI) alone should exceed the current account deficit, which should be an easily financed 1.0 percent of GDP. In January of this year, Heineken, Europe's largest brewery, acquired operations of FEMSA in Mexico, Latin America's largest beverage company. That investment alone exceeded the US$11.4 billion of DFI for 2009. This year, DFI is likely to exceed US$20 billion. The danger to the exchange rate will come from the international financial system and the wild card presented by market preoccupation with the "PIGS" (Portugal, Ireland, Italy, Greece and Spain). If the crisis that now looks tamed were to break out again or there were to be a sovereign default, all currencies would be vulnerable to a run like that experienced a year ago.

The tax increases that went into effect this year highlight the constraints the country faces. At a time when an expansive fiscal policy is most indicated, the extent of the fiscal stimulus is constrained by the structure of the government's finances. On the income side, Mexico relies on oil income to substitute for the low percentage of GDP paid in taxes. On the expenditures side, the quality of government spending and the costs of the massive growth of the state 30 years ago, now reflected in the form of pension obligations, ensure a growing need for income.

This time around, governments didn't squander the oil bonanza the way it was wasted in the 1970's and early 1980's. Part of the extraordinary income went to reduce the public sector's debt. However, much went to financing a boom in spending by state and local governments. Such spending has not been particularly transparent or subject to much accountability and, in too many instances, it has been of questionable utility.

Growth and job creation are Mexico's major immediate economic challenges. In order to absorb new entrants to the labor force, a sustained annual growth rate approximating 7 percent will be needed. Even under the most optimistic scenarios, growth will be far less than that. Boosting the sustainable long-term growth to 7 percent requires changes that Mexico's elite have shown little willingness to make. Until the longstanding reform agenda that would begin to erode the corporatist structure that dominates the country's polity and economy is implemented, the future of Mexico's economy will be characterized by mediocre growth, inadequate job creation, and a public sector ravenous for income.

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Mexico Consensus Economic Forecast
1st Quarter 2010 Summary

On the road to recovery

With the first quarter of 2010 nearing an end, there are signs that the Mexican economy continues upon the early phases of a recovery. According to recently released INEGI figures, inflation adjusted GDP increased during the final quarter of 2009, marking an increase of 3.9 percent from the previous three months. Given the recent improvements in aggregate output, the consensus outlook now paints a slightly more optimistic picture regarding expectations for Mexico's national economy. Despite the uncertain pace of short-term economic recovery, moderate growth in the U.S. economy should help bolster macroeconomic performance south of the border.

In the current quarter, the panelist's expectations for real gross domestic product (GDP) call for an increase of 3.5 percent in 2010. This represents an increase of nearly a full percentage point relative to last quarter's projection. Here, there is little disagreement among the panelists, with only one individual forecast calling for an increase in excess of 4 percent. The forecast scenario for aggregate output is driven in large part by the outlook for private consumption. Mexican consumers are now expected to increase their expenditures by nearly 3 percent throughout the course of this year.

As the pace of Mexican economic recovery remains tenuous in the short term, fiscal stimulus outlays will likely continue. However, taking into consideration current fiscal constraints in Mexico, government consumption is not likely to increase by more than 2 percent throughout 2010. During the same period, upswings in key indicators along with a generally improving commercial environment should help bolster confidence in Mexican business performance. As those trends unfold, the panelist consensus now calls for an increase in total fixed investment of 4 percent.

North of the border, growth in key sectors will likely fuel the demand for Mexican manufactured goods. In particular, an increase in U.S. industrial production activities will help total exports in 2010 rise by 8.4 percent according to the consensus. Mexican imports of goods and services are also forecast to increase sharply. In the coming months, imports prices are likely to remain steady as the result of a relatively tranquil exchange-rate. As the Mexican peso appreciates, and major sectors of Mexico's economy continue thier rebound, the panel now expects total imports to display annual growth in excess of 9 percent for 2010.

The rate of inflation is forecast to outpace levels previously anticipated. For 2010, seven of the nine panelists now expect consumer prices to rise by no less than 5 percent, while one projection calls for an increase of 6 percent. This quarter, the consensus figure calls for an annual increase in consumer prices of 5.3 percent. Representing a moderate improvement from the previous quarter's projections, the panel now expects the peso to appreciate to 13.14 P/$ for all of 2010.

This quarter, the panelists expect the yield on 28-day Treasury Certificates (CETES) to moderate slightly. The current consensus outlook calls for a 50 basis point drop in the 28-day CETES relative to the previous forecast. Similar to the previous quarter, this reflects the comparatively neutral policy stance of Mexico's central bank.

This quarter's consensus outlook calls for the moderate economic recovery taking hold in 2010 to continue through the end of next year. Growth in inflation-adjusted GDP is forecast to reach 3.5 percent for 2011, marching in step with the annual growth anticipated in 2010. Private consumption is forecast to grow at a slightly increased clip and increase by 3.2 percent. The forecast panel also expects the rate of increase for government expenditures to increase moderately. As major sectors of the Mexican economy regain steam paving the way for enhanced business conditions, fixed investment in 2011 is forecast to rise by more than 6.5 percent. Given this forecast economic climate, Mexico's imports and exports will continue to rise, albeit at rates slightly lower than those forecast for the current year. As these trends unfurl, consumer prices are forecast to rise by 4.2 percent in 2011, according to the consensus figure. However, throughout the course of the same twelve-month period, the panelists anticipate the Mexican peso to moderate slightly and rest at 13.39 P/$. According to the panel, in 2011 the 28-day CETES rate will increase to 6 percent.

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2010 Mexico Consensus Economic Forecast **Annual Average**

Annual Percent Change, 2010 from 2009

	GDP	Private Consumption	Government Consumption	Total Investment	Exports	Imports	Consumer Price Index	Exchange Rate	CETES 28 Day
American Chamber Mexico	3.6	3.2	2.5	5.8	9.4	10.6	5.2	13.00	4.7
JPMorgan Chase Bank	4.5	3.8	1.8	2.2	14.5	14.5	5.4	13.00	5.3
BBVA Bancomer	3.8	4.2	0.4	3.7	4.6	6.3	5.3	13.00	4.5
Wells Fargo Bank	3.4	3.1	3.0	5.2	8.3	6.7	4.5	12.75	4.5
Center for Economic Forecasting of Mexico	3.8	3.2	2.8	5.5	6.5	7.2	5.3	12.85	5.0
UACJ	3.0	3.0	2.0	2.0	3.1	6.0	5.2	14.00	6.0
ITESM	3.5	3.0	3.0	4.0	7.0	10.0	5.0	13.00	5.0
COLEF	3.2	1.5	2.0	3.0	10.0	10.5	6.0	13.10	5.8
UAdeC	3.0	0.8	0.6	5.0	12.0	12.0	5.5	13.60	5.5
Consensus -- this quarter	3.5	2.9	2.0	4.0	8.4	9.3	5.3	13.14	5.1
-- last quarter	2.6	2.4	2.0	3.4	8.8	8.4	4.8	13.31	5.6

2011 Mexico Consensus Economic Forecast **Annual Average**

Annual Percent Change, 2011 from 2010

	GDP	Private Consumption	Government Consumption	Total Investment	Exports	Imports	Consumer Price Index	Exchange Rate	CETES 28 Day
American Chamber Mexico	3.8	2.7	1.1	6.2	7.6	10.5	3.8	13.17	6.0
JPMorgan Chase Bank	3.5	5.4	2.2	14.0	9.0	14.4	4.0	13.00	7.0
BBVA Bancomer	3.6	2.1	0.2	5.2	7.5	3.4	3.8	13.00	6.2
Wells Fargo Bank	3.5	3.4	2.0	5.5	7.7	6.9	4.0	12.83	4.6
Center for Economic Forecasting of Mexico	4.5	4.2	4.0	7.8	7.5	8.5	4.7	13.20	6.0
UACJ	3.2	3.5	2.5	5.0	4.0	8.0	4.0	14.50	7.0
ITESM	4.0	4.0	7.0	5.0	8.0	12.0	4.0	13.00	6.0
COLEF	1.9	2.0	1.5	3.2	7.0	7.5	5.2	14.00	4.8
UAdeC	3.2	1.8	0.5	7.9	10.5	9.2	4.3	13.80	6.0
Consensus -- this quarter	3.5	3.2	2.3	6.6	7.6	8.9	4.2	13.39	6.0
-- last quarter	na	na	na	na	na	na	na	na	na

Annual Averages

Historical Data		GDP (2003 Pesos, billions)	Private Consumption (2003 Pesos, billions)	Government Consumption (2003 Pesos, billions)	Total Investment (2003 Pesos, billions)	Exports (2003 Pesos, billions)	Imports (2003 Pesos, billions)	Consumer Price Index June 02 = 100	Nominal Exchange Rate Pesos/ Dollars	CETES 28 Day
2009		8249.0	5820.0	953.0	1886.0	2290.0	2561.0	136.04	13.51	5.39
	Percent Change	-7.61%	-6.43%	2.42%	-8.03%	-15.50%	-16.24%	5.29%	21.27%	
2008		8,928.6	6,220.0	930.5	2,050.6	2,710.2	3,057.6	129.2	11.14	7.68
	Percent Change	1.35%	1.54%	0.59%	4.94%	1.40%	4.29%	*5.13%*	*1.92%*	
2007		8,809.9	6,125.5	925.0	1,954.0	2,672.9	2,931.7	122.9	10.93	7.19
	Percent Change	*3.33%*	3.86%	2.14%	7.17%	*5.66%*	*7.00%*	3.97%	*0.28%*	
2006		8,526.0	5,897.8	905.6	1,823.3	2,529.7	2,740.0	118.2	10.90	7.19
	Percent Change	*5.13%*	*5.68%*	*1.72%*	*9.78%*	*10.94%*	*12.57%*	3.63%	*-0.16%*	
2005		8,110.2	5,580.7	890.3	1,660.8	2,280.3	2,434.0	114.1	10.92	9.20
	Percent Change	*3.21%*	*4.78%*	*2.44%*	*7.46%*	*6.75%*	*8.48%*	*3.99%*	*-3.29%*	
2004		7,857.7	5,326.0	869.1	1,545.5	2,136.1	2,243.8	109.7	11.29	6.82
	Percent Change	*4.00%*	*5.62%*	*-2.76%*	*8.01%*	*11.50%*	*10.74%*	*4.69%*	*4.63%*	
2003		7,555.8	5,042.8	893.8	1,430.9	1,915.8	2,026.2	104.8	10.79	6.23
	Percent Change	*1.35%*	*2.22%*	*0.80%*	*0.37%*	*2.70%*	*0.70%*	*4.55%*	*12.05%*	
2002		7,455.0	4,933.1	886.7	1,425.6	1,865.5	2,012.2	100.2	9.63	7.09
	Percent Change	*0.83%*	*1.59%*	*-0.33%*	*-0.64%*	*1.44%*	*1.46%*	*5.03%*	*3.10%*	
2001		7,393.9	4,856.1	889.6	1,434.8	1,839.0	1,983.2	95.42	9.34	11.31
	Percent Change	*-0.16%*	*2.48%*	*-1.98%*	*-5.64%*	*-3.60%*	*-1.63%*	*6.36%*	*-1.27%*	
2000		7,405.5	4,738.7	907.6	1,520.5	1,907.6	2,016.1	89.71	9.46	15.24
	Percent Change	*6.60%*	*8.18%*	*2.38%*	*11.36%*	*16.28%*	*21.47%*	*9.50%*	*-1.05%*	
1999		6,946.9	4,380.3	886.5	1,365.4	1,640.5	1,659.7	81.93	9.56	21.41

Note: 2009 data are preliminary and subject to revision

*GDP: Producto Interno Bruto, INEGI, 2003 Pesos
*Private Consumption: Consumo Privado, INEGI, 2003 Pesos
*Government Consumption: Consumo de Gobierno, INEGI, 2003 Pesos
*Total Investment: Formacion bruta de capital fijo, INEGI, 2003 Pesos
*Exports: Exportacion de bienes y servicios, INEGI, 2003 Pesos
*Imports: Importacion de bienes y servicios, INEGI, 2003 Pesos
*CPI, Banco de Mexico, Annual Average, Base = June 2002
*Exchange Rate, Banco de Mexico, Peso-to-dollar, Fecha de Liquidacion, Annual Average
*CETES 28 Days, Banco de Mexico, Annual Average

México Consensus Economic Forecast, a quarterly publication of the Border Region Modeling Project, a research unit within the Department of Economics & Finance at the College of Business Administration of The University of Texas at El Paso, is available on the Web at: **http://academics.utep.edu/border**. Econometric research assistance is provided by Enedina Licerio and Teodulo Soto. For additional information, contact the Border Region Modeling Project - CBA 236, UTEP Department of Economics & Finance, 500 West University Avenue, El Paso, TX 79968-0543, USA. (915) 747-7775.