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Mexico Consensus Economic Forecast

Alejandro Díaz-Bautista
El Colegio de la Frontera Norte

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CONSENSUS ECONOMIC FORECAST

MÉXICO

University of Texas at El Paso
Border Region Modeling Project

4th Quarter 2009

American Chamber México
Dr. Deborah L. Riner

Wells Fargo Bank
Dr. Eugenio J. Alemán

Center for Economic Forecasting of Mexico
M.A. Rodrigo Pulido

JP Morgan Chase Bank
Dr. Alfredo Thorne

BBVA Bancomer
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Pedro Uríz
Cecilia Posadas

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Dr. Jorge Ibarra Salazar

Universidad Autónoma de Coahuila
Dr. Alejandro Dávila Flores

Mexican Economic Fluctuations in 2009

Mexico was one of the first casualties of the international financial meltdown that emerged during the third quarter of 2008. Peso instability materialized very quickly as multiple sources of currency inflows quickly dried up. Some of the currency inflows came from non-traditional sources.

At the start of the U.S. economic downturn, many of the first workers to lose their jobs were immigrants in the construction and service industries. That quickly translated into a reduction in remittances sent to families in Mexico. For all of 2008, remittances totaled $15,553 million USD, a decline of 4.2 percent relative to 2007. For 2009, family transfers are expected to weaken further and fall by nearly 10 percent.

Echoing earlier economic recessions, the current downturn has been accompanied by reduced levels of undocumented immigration to the United States and increased deportations of prior migrants. Historically, those developments have always presaged lower transfers for periods that extend beyond the official end points of macroeconomic contractions.

Not surprisingly, unemployment has increased in Mexico. Data from the monthly National Survey of Occupation and Employment (ENOE) conducted by INEGI (the national statistics agency) reached 6.4 percent in September 2009, more than 200 basis points above the jobless rate from 12 months earlier. Manufacturing payrolls have started to recover in response to greater industrial activity in the United States, so unemployment may be at or near its cyclical peak. Domestic financial and retail sector performances should strengthen once labor market conditions begin to improve.

Increased economic integration with the United States has caused the effects of the downturn to be felt more severely in Mexico than was the case in prior decades. North of the border financial uncertainty in 2009 has also contributed to high levels of volatility in the stock market in Mexico, as well as notable currency market jitters. To prevent unnecessary foreign exchange gyrations for the peso, the central bank instituted a daily auction system that has helped stabilize the currency market by insuring that liquidity is present on a day-to-day basis. The availability has been impacted by numerous factors, including a 24 percent decline in direct foreign investment, to US$9.976 billion, during the first half of 2009.

Complicating matters is the decline in energy prices that began in August 2008. Lower export prices for petroleum affect the current account as well as the fiscal budget. Concerns exist that the US$59 per barrel estimate embodied in the 2010 federal budget may prove optimistic. If that is the case, then budget cuts similar to those of 1998 may have to be enacted.

Mexico is not expected to begin to recover from the current downturn until the second half of 2010. Growth that year may reach only 2 percent. The projected 7.1 percent decline this year means that this recession is likely to be deeper than that of 1995. While definitely not an appealing prospect, several key indicators have begun to improve, indicating that the foundations for better performance may already be in place. Consumers and businesses alike are more than ready for some good news along those lines.

Dr. Alejandro Díaz-Bautista
El Colegio de la Frontera Norte

Mexico Consensus Economic Forecast
4th Quarter Summary

Light at the end of the tunnel?

For 2009 as a whole, this quarter's consensus outlook anticipates a steep decline of 6.9 percent in real gross domestic product (GDP). This outlook for inflation-adjusted GDP is not surprising given the panelists expectations for private consumption, as consumers are expected to reduce expenditures by 6.5 percent this year alone. Projections for the government stimulus package have declined substantially, however, with government consumption growth expected to slow to less than 1 percent. Diminished confidence in the Mexican business sector is still expected to cause total fixed investment to shrink at double digit rates. Given the lingering effects of the global economic downturn, the panelists also expect imports and exports to display steep contractions in excess of 11 and 22 percent, respectively. The 2009 consensus figure calls for consumer price increase in excess of 4 percent. Against this backdrop, the panelists expect a 2009 average exchange rate of 13.42 pesos per dollar. Over the same course, the consensus outlook for the 2009 yield on 28-day Treasury Certificates (CETES) holds steady at 5.5 percent, again, this quarter.

There are several signs that the turbulence in Mexico's economy brought upon by the global recession is abating. The latest government data reported by INEGI indicate that inflation-adjusted GDP in Mexico grew during the third quarter of 2009. Formal sector payrolls have started to expand in many metropolitan economies across the country. Along with those developments, the peso has strengthened in recent weeks. While the rate at which economic gains unfurl in Mexico remains to be seen, sustained recovery will be largely dependant upon national business cycle advances, or declines, in the United States.

As 2009 comes to an end, the current consensus outlook calls for the Mexican economy to turn the corner towards recovery in 2010. While the consensus calls for improvements in several key indicators, caution is the rule of the day. Real GDP is now expected to grow by 2.6 percent, a 30 basis point improvement from last quarter's survey. Private consumption is similarly forecast to increase by a moderate 2.4 percent next year.

Although fiscal stimulus efforts are likely to continue in early 2010, budgetary pressures are expected to reign in government expenditures, limiting their growth to only 2.0 percent. Despite forecast improvements in the Mexican business climate, some uncertainty regarding cash flows and overall profitability persists. Given the latter, two of the nine panelists anticipate additional contraction in fixed investment levels. However, the consensus projection suggests that a generally improved business environment will allow total fixed investment to increase by 3.4 percent in 2010.

Upswings in north of the border industrial production will bolster Mexico's intra-industry exports. The panel now anticipates exports will rise by 8.8 percent next year, 210 basis points above what was forecast last quarter. The consensus outlook for imports of goods and services produced abroad has grown by an even larger amount to 8.4 percent. The latter is partially due to greater demand for intermediate inputs in manufacturing, as well as both real and nominal appreciation in the peso. Enhanced macroeconomic conditions help the Mexican peso appreciate moderately to 13.38 P/$.

This quarter, the consensus paints a slightly different picture for inflation. Consumer prices are now forecast to increase by 4.8 percent, nearly a percentage point greater than the previous quarter's projection. In spite of the uptick in the CPI, credit conditions are not expected to tighten very much. The panel anticipates the yield for 28-day Treasury Certificates (CETES) to remain relatively unchanged in 2010. With Mexican monetary policy remaining comparatively neutral, the consensus now expects the rate of return for these instruments to rest at 5.6 percent for 2010 as a whole.

From a cyclical perspective, the big question facing Mexico is one that falls beyond the reach of its policy makers. Namely, will the United States avoid a double dip back into recession as commercial real estate loans come due? From a structural perspective, the big question looming over 2010 is whether congressional leaders in Mexico City will begin introducing badly needed reforms in areas such as the labor code, business licensing requirements, the tax code, and the energy sector. Failure to do so will eventually lead to further credit score downgrades by the major rating agencies.

Thomas M. Fullerton, Jr. and Angel L. Molina, Jr.
University of Texas at El Paso Border Region Modeling Project

2009 Mexico Consensus Economic Forecast

Annual Percent Change, 2009 from 2008 — **Annual Average**

	GDP	Private Consumption	Government Consumption	Total Investment	Exports	Imports	Consumer Price Index	Exchange Rate	CETES 28 Day
American Chamber Mexico	-7.0	-7.2	1.6	-10.5	-24.1	-25.4	4.0	13.56	5.4
JPMorgan Chase Bank	-7.0	-7.1	3.0	-16.0	-20.0	-22.0	4.0	13.00	4.5
BBVA Bancomer	-7.2	-7.7	1.7	-11.2	-20.8	-24.0	4.0	13.50	5.4
Wells Fargo Bank	-6.9	-7.2	1.3	-9.8	-16.1	-17.5	5.3	13.51	5.4
Center for Economic Forecasting of Mexico	-6.8	-6.6	-0.5	-9.7	-16.5	-17.0	4.0	13.50	5.5
UACJ	-6.2	-4.0	1.2	-15.0	-25.0	-20.0	4.0	13.50	5.4
ITESM	-7.0	-6.0	2.0	-10.0	-35.0	-25.0	4.0	13.50	4.5
COLEF	-7.0	-5.8	-3.7	-7.5	-26.8	-23.7	5.9	13.20	7.8
UAdeC	-7.0	-7.0	1.5	-11.5	-21.0	-22.0	5.4	13.50	5.5
Consensus -- this quarter	-6.9	-6.5	0.9	-11.2	-22.8	-21.8	4.5	13.42	5.5
-- last quarter	-7.1	-6.9	2.3	-11.8	-20.1	-20.3	5.0	13.39	5.5

2010 Mexico Consensus Economic Forecast

Annual Percent Change, 2010 from 2009 — **Annual Average**

	GDP	Private Consumption	Government Consumption	Total Investment	Exports	Imports	Consumer Price Index	Exchange Rate	CETES 28 Day
American Chamber Mexico	3.0	2.7	1.0	5.8	8.6	9.4	4.8	13.36	5.2
JPMorgan Chase Bank	3.5	3.2	1.0	6.1	15.0	14.0	5.1	13.00	5.3
BBVA Bancomer	3.1	3.2	2.7	-0.3	2.2	1.5	5.2	13.00	4.5
Wells Fargo Bank	2.9	3.1	2.3	2.9	3.4	3.3	3.7	12.97	4.6
Center for Economic Forecasting of Mexico	3.5	2.9	0.5	4.5	3.5	4.2	5.5	13.00	5.1
UACJ	2.5	2.0	1.0	5.0	5.5	6.0	5.2	14.10	7.0
ITESM	3.0	2.0	7.0	5.0	10.0	10.0	4.3	13.30	5.5
COLEF	-0.5	0.5	1.2	-2.5	25.0	22.0	5.1	13.50	8.1
UAdeC	2.5	2.0	1.5	4.5	6.0	5.5	4.5	13.60	5.5
Consensus -- this quarter	2.6	2.4	2.0	3.4	8.8	8.4	4.8	13.31	5.6
-- last quarter	2.3	2.0	1.8	4.8	6.7	3.8	3.9	13.38	5.2

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)	CPI June 2002 = 100	Nominal Exchange Rate Pesos/ Dollars	CETES 28 Day
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: 2008 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: Formación Bruta de Capital Fijo, INEGI, 2003 Pesos

*Exports: Exportación de Bienes y Servicios, INEGI, 2003 Pesos

*Imports: Importación de Bienes y Servicios, INEGI, 2003 Pesos

*CPI, Banco de México, Annual Average, Base = June 2002

*Exchange Rate, Banco de México, Peso-to-Dollar, Fecha de Liquidación, Annual Average

*CETES 28 Days, Banco de México, 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.