SNAPSHOT U.S. - Mexico

Macroeconomic Snapshot

May 2011

GROWTH: Excluding 2009's negative 6.1 growth, GDP in recent years has averaged about 3.5%. Given that Mexico is so integrated into the U.S. business cycle, the global financial and economic crisis in 2008 hit the country's real economy harder than any other emerging economy. A surge in exports to the U.S., particularly of the automobile industry, boosted the economy, which grew 5.5% in 2010. The Mexican economy is expected to grow 4.6% in 2011. The missing structural reforms, an escalation of drug-related violence, as well as issues that could arise from European periphery countries, and the possibility of less vigorous U.S. growth remain the main risks to Mexico's growth outlook.

Unlike most industrialized economies, the Mexican government maintained its fiscal deficit relatively low at 2.8% of GDP in 2010, and will return to a balanced budget –with a zero fiscal deficit- by 2012. To protect the economy from external shocks, the government renewed its IMF flexible credit line for $73 billion for two more years and the central bank implemented a dollar-auction mechanism to increase international reserves, which have grown from $91 billion in 2009 to $123 billion. Low global inflation, peso appreciation, stronger competition among retailers, and a still negative output gap helped keep inflation under control. Annual inflation in 2010 totaled 4.32%, slightly above the central bank's 3% (±1) target. The central bank expects annual inflation to converge towards its 3% (±1) target in the 3Q11. Since July 2009, the central bank has kept its benchmark lending rate steady at 4.5%.

The unemployment rate in 2010 was 5.4%, down from the 5.5% registered for 2009. Although 730,000 formal jobs were created during 2010, supply has failed to meet demand as over one million job-seekers have entered into the labor market (and will continue to do so each year). About 29% of the employed population (or 12 million people) work in the informal sector.

The global crisis and escalating public insecurity have negatively impacted FDI, which fell from $25.8 billion in 2008 to $15.2 billion in 2009. FDI recovered in 2010 and reached $18.7 billion. FDI from the United States represented 28% of the total. FDI is expected to reach between $17 billion and $19 billion in 2011.

INTERNATIONAL TRADE: As a percentage of GDP, Mexico's exports have risen from 12% in 1993 (before NAFTA) to approximately 30% in recent years. Depite Mexico's extensive network of FTAs (covering 80% of the world economy), over 80% of export are to the United States. Mexico is the third largest U.S. trading partner, following Canada and China, and the third largest U.S. source of imports after China and Canada. In 2010, Mexico's export growth to the U.S. was 30%, surpassing China and Canada's growth of 23% and 22%, respectively. Mexico's major exports to the United States are electrical goods (39%), cars/auto parts (14%) and oil (11%).

POVERTY: According to the most recent poverty measures (2008), Mexico's overall poverty rate is 44.2% or 47 million people, but the indicators show that 70% of Mexicans lack at least one of the eight basic needs identified in the new multidimensional system. The new measurements, based on a 2008 survey, show that 36 million Mexicans (33.7%) live in moderate poverty, and 11.2 million (10.5%) live in extreme poverty. Mexico's considerable wealth is not evenly distributed among its people. The southern region is by far the poorest area of the country. The northern states of Nuevo Leon, Baja California, and Coahuila, are among the richest states. The lack of economic opportunities – specifically decent jobs – for poor Mexicans is a major driver of migration – both internal and international – and exposes Mexico's poorest people to increased vulnerability and marginalization.

ENERGY: The oil sector is a critical component of the Mexican economy: crude oil accounts for about 5-6% of GDP, 10-15% of exports and 30-40% of fiscal revenues. Due to the decline of Mexico's largest oil field –Cantarell- and underinvestment in new exploration and exploitation, crude oil production has declined rapidly from a peak of 3.4 million barrels per day in 2004 to a projected 2.5 million barrels per day in 2011. The Calderon administration was able to pass an energy reform, which the Congress approved in 2008. The reform allowed Pemex to sign "performance contracts" with private companies for oil exploration and production activities, but without sharing oil or oil income.

FINANCIAL SECTOR: Thanks to the strengthening of the legal framework over the past few years, good asset risk management, and larger preventive reserves, banks remained solid and solvent with a low non-performing loan index and high capitalization levels during the past global crisis. Although only about 40% of Mexicans have commercial bank accounts, 60% have access to the financial system compared to only 25% in 2004. However, credit penetration in rural areas remains low. About 64% of Mexico's 2,456 municipalities do not have a branch bank. While large firms continue to have access to credit, SMEs report access to credit as a key barrier to growth.

COMPETITIVENESS: Mexico ranks 66th in the most recent World Economic Forum Global Competitiveness Index 2010-2011, out of 132 countries, down six places from its previous rank in 2009. Mexico improved its ranking in the 2011 World Bank's Doing Business report from 41st to 35th, largely due to the reduction of days required to open a new business. The most problematic factors for doing business are: inefficient government bureaucracy, corruption, access to financing, and crime and debt.

REFORMS: The Calderon administration passed a fiscal reform in 2009 aimed at strengthening public finances in the medium term, but Mexico's narrow tax base, the government's heavy reliance on oil revenues and the oil output decline still exercise significant pressure on public finances. The Calderon administration also succeeded in passing a pension reform, an energy reform, as well as an agreement endorsed by the powerful teachers' union to enhance the quality of education. However, to assure Mexico's ability to compete worldwide, the government still needs to tackle a series of structural reforms to increase the country's competitiveness including more comprehensive energy and education reforms; a labor reform that reduces the cost of doing business in the formal sector, as well as broader financial inclusion, and improved intellectual property rights protection.