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Economics Group

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More Light on Mexican 2016 GDP: The Demand Side

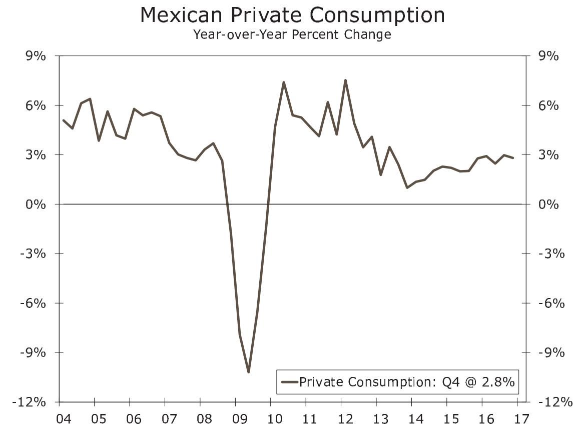
The Mexican economy in 2016 was supported by a relatively strong consumer sector with personal consumption expenditures increasing 2.8 percent during the year.

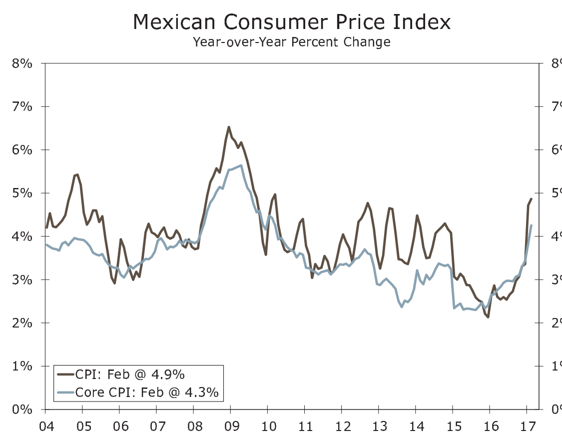
Can Consumer Demand Continue to Grow at These Rates?

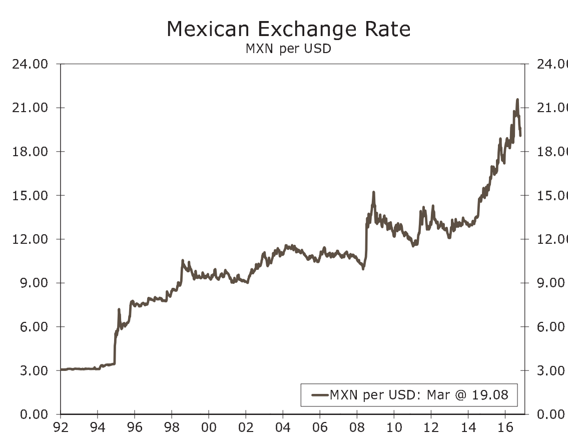
Our forecast for a mild recession for the Mexican economy this year rests on our expectation that the strength shown by the Mexican consumer during the past several years cannot continue for much longer. In fact, personal consumption expenditures' (PCE) contribution to GDP growth in 2016 was an impressive 1.9 percentage points. This means that PCE growth represented almost 83 percent of the 2.3 percent growth in the economy in 2016. Other contributors to economic growth were government consumption and gross fixed capital formation, both contributing 0.1 percent to 2016 economic growth, and export and imports of goods and services, both contributing 0.4 percent to economic growth (recall that imports enter GDP with a negative sign). That is, the weakness in real import growth was good for economic growth in 2016. Had import growth been higher, then PCE would have been the only game in town.

Thus, the question is: How long can Mexican consumers continue to support the economy if production is so weak? This is probably the question that will need to be answered in the first half of 2017. And, what has happened to inflation during the first quarter of the year will probably have a lot to do with the answer. Consumer prices skyrocketed early in the year, to 4.9 percent year-over-year in February from a year-over-year rate of 2.9 percent in February 2016, as the Mexican government "adjusted" gasoline prices (i.e., increased gasoline prices by 20 percent). Recall that Mexican gasoline prices are regulated by the government and are normally used as a tax on higher income households, which are the ones that are able to buy cars. Furthermore, the lack of refining capacity from the country's refineries has pushed the country to import a large amount of gasoline, mostly from the United States. Thus, the large depreciation of the currency put pressure on fiscal accounts and the Peña Nieto administration decided to increase the price of gasoline to reduce this pressure.

The increase in the price of gasoline gave rise to large social upheaval during the first quarter of the year, and our estimation is that consumer demand weakened considerably during the quarter. Thus, the almost doubling of the rate of growth in consumer prices early in the year plus the large depreciation of the currency will have its impact on consumer demand during the first quarter of the year. Furthermore, our estimate of a more than doubling of consumer prices in 2017, from 2.8 percent to 6.7 percent, will keep the pressure on consumer demand for the rest of the year and prevent the economy from outperforming our forecast. In addition, we have to add the uncertainty generated by President Trump's policies toward Mexico, which will likely continue to hurt production.







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