

Regional Economic Report

July – September 2013

Summary

Economic activity in all regional economies observed an incipient recovery in the third quarter of 2013 over the previous quarter. The recovery was mainly driven by the dynamism of the manufacturing sector, which responded to a better performance of external demand.¹ In turn, domestic demand kept presenting mixed signals, with a noteworthy weakness of sales' and construction indicators in all regions. By the end of the reference quarter, the hurricanes "Ingrid" and "Manuel" moderately affected the economic activity, primarily in the agricultural sector, which presented a differentiated performance by region.

The rebound in the manufacturing activity in the third quarter of 2013 was supported by both a better performance of the non-automobile manufacturing exports to the U.S. and an upward trend in the automobile exports, to the U.S. and the rest of the world. Business agents of different economic sectors interviewed by Banco de México for this Report pointed out, especially in the Northern, North-Central and Central regions, the link between the performance of the automobile industry and that of their respective regions. To deepen the comprehension of this relation, a Box in this Report presents a study of the pattern of this industry's regional development. The analyzed indicators show that the automobile industry is characterized by its geographic concentration and that it has managed to consolidate the formation of clusters. The favorable evolution of the automobile sector, despite the slowdown in the external demand during the previous quarters, indicates that fostering agglomeration economies and, therefore, increasing productivity contributes to making regional economies more resilient to economy-wide shocks. According to the interviewed business agents of the automobile sector, public policies fostering the development of human capital and the provision of infrastructure in their regions are key elements in supporting the formation of clusters.

During the third quarter of 2013, annual headline inflation in all regional economies maintained the downward trend, which had begun in the second quarter. This was contributed to by a favorable performance of both the core and non-core component. The downside trajectory of annual core inflation resulted from a lower inflation of the merchandise

subindex and from the low level at which the inflation of the services' subindex persisted. The reduction of annual non-core inflation was motivated by the fading of the shocks in the agricultural products' prices at the end of the first quarter of 2013.

The business contacts interviewed by Banco de México for this Report generally stated that in all regional economies a further recovery of the demand for own goods and services over the following six and twelve months is anticipated. This expectation is mainly supported by the reactivation of domestic demand, derived from a greater dynamism of public expenditure, particularly that associated to the Transport and Communications Infrastructure Investment Program of the Mexican Government, as well as a moderate growth of external demand. Nonetheless, in all regions the abovementioned business agents cited different factors as downward risks, both external and domestic, to the economic expansion. Among the former, a lower than anticipated growth rate of the U.S. economy and the possibility of new volatility episodes in international financial markets were mentioned. Among the latter, the smaller than foreseen impulse generated by the structural reforms, the persistence of the weak private construction for a longer than anticipated period, deterioration in perceived public safety and the occurrence of adverse weather phenomena were reported.

Finally, regarding inflation expectations, the interviewed business agents revealed that no significant inflationary pressures on salary costs are anticipated over the following six and twelve months, given that a considerable slack in regional labor markets is expected to prevail over this period. As regards input prices, lower rates of their annual change are generally expected. In line with the abovesaid, they also expect a lower growth rate of sales prices. And, lastly, the interviewed business agents expect the impact of the fiscal modifications on inflation to be transitory and moderate in their respective regions in 2014.

¹ Regionalization: Northern: Baja California, Sonora, Chihuahua, Coahuila, Nuevo León and Tamaulipas; North-Central: Aguascalientes, Baja California Sur, Colima, Durango, Jalisco, Michoacán, Nayarit, San Luis Potosí, Sinaloa and Zacatecas; Central: Distrito Federal, Estado de México, Guanajuato, Hidalgo, Morelos, Puebla, Querétaro and Tlaxcala; and Southern: Campeche, Chiapas, Guerrero, Oaxaca, Quintana Roo, Tabasco, Veracruz and Yucatán.