

Regional Economic Report

April – June 2013

Summary

During the second quarter of 2013 economic activity weakened in all regional economies. In particular, commercial activity contracted and construction, especially housing construction, remained stagnant.

With respect to manufacturing production, it contracted in the Central region. On the other hand, activity in the tourism sector and funding to firms strengthened in all regions of Mexico.¹ According to business agents interviewed by Banco de México for this Report, the deterioration of the economic activity in the reference quarter in all regions was consequent on the slowdown of the world economic growth and lower dynamism of domestic demand, especially of public expenditure and activity in the construction sector.

As regards employment, the growth rate of IMSS-insured workers continued decelerating in the second quarter of 2013 in all regional economies. This slowdown, which had been observed since mid-2012, as a response to shocks affecting the economy, accentuated in the Northern and Southern regions. These regional differences can be partly attributed to two elements: on the one hand, the degree of regional economies' exposure to the different shocks, and, on the other hand, the way in which labor markets adjust to a lower labor demand at the local level. The former factor was analyzed in the Box of the Regional Economic Report April-June 2011, where the degree of synchronization between the economic cycles of the regions in Mexico and that of the U.S. was examined. The latter factor is analyzed in a Box of this Report. The main result of the analysis is that the adjustment to a negative shock to local labor demand is initially accounted for by a lower labor participation rate. Subsequently, worker mobility to other states takes on greater relevance in explaining the adjustment in the local labor market. Thus, the differences recently observed across regions in the variation of the employment growth rate seem to be mainly due to the changes in the labor participation rates of each region.

Regarding annual headline inflation, following an uptick at the end of the first quarter of 2013 and the beginning of the second one, in May it began a downward trend in the Central and Southern regions, and from June onwards, in the Northern and North-Central regions as well. These annual headline inflation dynamics were mainly due to the evolution of inflation in some

agricultural products' prices of the non-core component. On the other hand, annual core inflation presented a downward trend over the period covered by this Report, locating in August 2013 at historical minimum levels in the four regions of Mexico.

The interviewed business agents anticipate over the next six and twelve months an expansion of demand for own products and services, and they generally expressed greater optimism for the one-year horizon. The expected expansion is principally supported by two forecasts: on the one hand, regarding external demand, the referred business agents emphasized that the evolution of the U.S. economy in general improved at the end of the second quarter of 2013, and that it will positively impact the economic activity in all regions in Mexico in the second half of the year; and, on the other hand, they anticipate the domestic demand to perform better than in the first half of 2013, as a consequence of a greater dynamism of public expenditure and, particularly, of a rebound in public works' construction.

In the four regions, the abovementioned business agents pointed out different risk factors, both upward and downward, to the economic activity in their respective regions. Among the upside risks they mentioned the possibility of further progress in the process of structural reforms, as well as a better than expected performance of external demand. Among the downside risks they noted the fact that the recovery of the U.S. economy could turn out weaker than estimated, an environment of further exchange rate volatility and the possibility that the public safety conditions could deteriorate. Additionally, in some cases they also mentioned as a downward risk the fact that the reactivation of public expenditure in the second half of the year could be weaker than expected.

The interviewed business agents announced that no significant inflationary pressures for the following six and twelve months are anticipated. Indeed, they mentioned that the low pass-through of exchange rate adjustments to inflation, increased competition, the technological change in the telecommunications industry, the expected grain production, weakness of world economic growth, and lower international commodity prices are the factors that will contribute to maintaining inflation at low and stable levels over the referred time period.

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.