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In early March, the Banco de Mexico (Central Bank) reported the consumer price index (Indice Nacional de Precios al Consumidor, INPC) increased by 2.33% during February. The INPC rate was slightly lower than that forecast by many analysts, who had anticipated an increase of about 2.5%. However, there was widespread concern about the accumulated figure of 6% for January-February, which cast strong doubts on President Ernesto Zedillo's ability to meet his targeted annual inflation rate of 20.5% this year. To meet that goal, monthly inflation in Mexico would have to average 1.7% between March and December. Last year, the Zedillo administration's forecasts for the annual inflation rate were overly optimistic, first projecting the annual increase at 16%. It then upped the forecast to 42%, following a decision to raise the value added tax (impuesto al valor agregado, IVA), effective in April.

In the end, the administration failed even to meet its 42% inflation goal, with 1995 annual inflation reaching close to 53%. Many private economists and even the Banco de Mexico have now dismissed the Zedillo administration's projections for a 20.5% inflation rate for this year. In an internal report, obtained by the daily newspaper La Jornada, the Banco de Mexico has forecast annual inflation for 1996 at 25%, or four percentage points above the administration's estimate. For their part, many private economists are forecasting the annual rate at 30% or higher. A significant concern regarding the February inflation statistics was the surge in the price of basic products, which could continue to be a liability for the governing Institutional Revolutionary Party (PRI), especially if prices continue to increase between now and key 1997 state and congressional elections.

According to the Banco de Mexico, the index for the basic basket of goods during February increased by 2.5% over January, which was slightly more than the INPC increase of 2.3% The accumulated January-February increase for the basic basket of goods was 7.25%, more than one percentage point higher than the INPC for the same two- month period. Meanwhile, a Finance Secretariat (SHCP) report said the highest increase for any category during February was in clothing and footwear, which rose by more than 3%, compared with January. Price increases were also reported for a wide range of consumer products and services, including domestic furniture and appliances, airline tickets, school supplies, medicines, telephone service, hospital fees, cigarettes, cosmetics, heating oil, automobile insurance, and gasoline.

As for food and beverages, the Banco de Mexico said consumers paid higher costs during February for such products as processed milk, cheeses, seafood, fresh meat, beans, sugar, flour, condiments, and sweets. According to the SHCP report, the greatest increases were reported in the cities of Tepic (Nayarit state); Ciudad Acuna (Coahuila), and Tijuana (Baja California). On the other hand, the smallest increases were reported in Tapachula (Chiapas), Matamoros (Tamaulipas) and Durango (Durango).

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The Banco de Mexico attempted to put a positive spin on the February statistics, pointing out that the February inflation rate was much lower than the INPC increase of 3.6% in January and 3.2% in December. Indeed, the Zedillo administration and members of the PRI are confident that the government will be able to keep the inflation rate low. In an interview with La Jornada, PRI president Santiago Onate Laborde expressed confidence that the latest anti-inflation and economic growth agreement (Alianza para la Recuperacion Economica, APRE) signed by representatives of labor, business, and the government late last year, will help keep the inflation rate under control long enough to allow the economy to stabilize this year and begin to grow next year. Still, despite forecasts of a 2% to 3% GDP decline for the first quarter of the year, the Zedillo administration continues to project a 3% overall growth in GDP for 1996. Many private economists, however, say the best-case scenario is that Mexico will attain a GDP growth of about 1.5% this year. In fact, many economists warn that the administration's efforts to limit inflation could backfire if the government does not tone down its GDP-growth forecasts.

"The Zedillo administration will have to lower its target for economic growth this year if it wants to bring inflation under control," said an article in the daily newspaper Excelsior. In a separate piece in Excelsior, columnist Sergio Miranda Gonzalez said the administration's overly optimistic predictions appear to be causing greater harm than benefit to the Mexican economy. "The lack of clear signals on whether the economic decline has reached a bottom or whether we are indeed in a moderate recovery phase has increased nervousness in the currency markets," said Miranda. He said this uncertainty will result in a continued undervaluation of the peso, which, in turn, will keep interest rates high.

According to some economists, higher inflation rates than originally anticipated will also mean that the Banco de Mexico will maintain a very restrictive monetary policy, which will boost interest rates and restrict economic growth. Additionally, there are no guarantees that labor unions and business leaders will stick to the commitments made under the APRE. The administration is receiving strong pressure to allow wage increases, beyond the 10% negotiated in the APRE in October of last year (see SourceMex, 11/01/95), to help boost the purchasing power of workers. The government is expected to accept an additional increase of 5% in the minimum wage. Nevertheless, business leaders are opposing any wage increases beyond those negotiated in the APRE.

Many business leaders warn that a generalized wage increase would be self- defeating, since this would have an adverse effect on the inflation rate in the long run. Meanwhile, the economic consulting company Consultores Internacionales predicted that the INPC will remain stable or drop slightly in March, but will resume an upward trend in April, when the 10% increase in the minimum wage and in the price of certain basic goods and services, negotiated under the APRE, are scheduled to be implemented. Some of the optimistic predictions of reductions in inflation during March are the result of a steady drop in producer prices over the past two months. According to the Banco de Mexico, the producer price index (Indice Nacional de Precios al Productor, INPP) increased by only 2.34% during February, compared with 3.59% in January and 3.26% in December 1995.

Still, Consultores Internacionales pointed out that producers of some basic products such as milk and tortillas are expected to keep pressure on the government to remove price controls on their products. If the government caves in to the pressure, this could potentially contribute to a surge in

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the inflation rate later in the year. (Sources: Agence France-Presse, 02/24/96, 03/01/96; El Financiero International, 03/04/96; Excelsior, 03/05/96, 03/08/96; El Norte, Reforma, 03/08/96; La Jornada, 03/08/96, 03/11/96)

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