Reforms Could Boost Mexican Economy, Which Has Showed Low Growth So Far in 2014

Carlos Navarro
Reforms Could Boost Mexican Economy, Which Has Showed Low Growth So Far in 2014

by Carlos Navarro
Category/Department: Mexico
Published: 2014-07-09

The Mexican economy could match the current average growth rate for the Organization for Economic Development and Cooperation (OECD) by the year 2050 if reforms to telecommunications, energy, and other sectors bring in the needed investments. That assessment from Mexico’s former finance secretary and current OECD secretary José Ángel Gurría Treviño does not take into consideration other factors that could derail growth, such as the government’s inability to control insecurity, which could deter foreign investment and cause Mexican companies to move their operations overseas. Mexico is one of 32 members of the OECD.

Speaking at a conference on global development in Paris, Gurría raised concerns about the low growth of emerging countries like Mexico, but he said he was confident that reforms would give the Mexican economy a boost. "This is not a question of optimism or pessimism," said the OECD secretary-general. "However, because of the reforms, the tendencies are going to change."

The Mexican Congress this year approved secondary legislation to implement reforms to the telecommunications sector (SourceMex, July 9, 2014). The enabling legislation for Mexico’s most important reforms, those in the energy sector, are still pending, and congressional leaders said those legislative initiatives could be approved in the next few weeks.

Estimates by the daily business newspaper El Financiero indicate that Mexico would have to attain an annual growth rate averaging 4.3% to match the average GDP rate of the OECD countries. This matches the outlook from the Secretaría de Hacienda y Crédito Público (SHCP), which foresees GDP growth of about 5% between 2015 and 2018, once reforms are in place.

Without the reforms, Mexico’s average growth rate is projected at about 2.5% between 2010 and 2060. "At this rate, Mexico would have to wait until 2016 to match the average GDP growth rate of the OECD," said El Financiero.

The GDP growth rate in the first quarter of the year lagged, in part because of slow growth in Mexico’s top trading partner, the US. The slow US growth, however, was not a deterrent to remittances from Mexican expatriates in the first part of 2014 (SourceMex, June 25, 2014).

The OECD said Mexico ranked 21st among the 32 OECD countries in growth during January-March of this year, reporting GDP growth of 0.3% during the period. This was an improvement from the 0.1% in the first quarter of 2013.

Among the OECD countries, the highest growth rates in January-March 2014 were recorded in Turkey, Japan, Australia, Hungary, and Poland. The lowest rates were recorded in the US, Estonia, and the Netherlands.
Some improvement expected in second half of 2014

The low growth rate during the first quarter of the year could keep the overall economy down in 2014, although some improvement is expected later in the year. Private forecasters expect Mexico’s GDP growth for 2014 to reach about 3% in 2014.

"Mexico is following the patterns of the US, and the US data for May and June showed an improvement," said Carlos Capistrán, an economist at the Bank of America Merrill Lynch office in Mexico City. "Our economists are following [this trend] closely, and anticipate a rebound of 4% for the second quarter and 3% thereafter."

Capistrán, who said Mexico’s economy would be driven by exports and government expenditures the rest of the year, projected a growth rate of 2.6% for all of 2014.

One factor that contributed to low growth in the first quarter of the year was the new tax reform that went into effect at the beginning of 2014, which imposed a uniform value-added tax (impuesto al valor agregado, IVA) of 16% throughout the country, closed loopholes for wealthier Mexicans, and applied a special consumption tax on soft drinks and junk food. (SourceMex, Sept. 18, 2013, and March 12, 2014). The tax increases have put some members of the business sector at odds with the Peña Nieto government.

"The impact of the tax increase was especially strong in the first quarter of the year, but the effect will subside. People will eventually become used to a system where the government keeps a larger amount of their earnings," columnist Sergio Sarmiento wrote in the daily newspaper Reforma. "Those who stopped drinking soft drinks or eating cereal for breakfast [because of new taxes] will resume their consumption habits."

"The deep problem for Mexico is the one that has always existed. We live in a system designed to inhibit productive investment in communal lands (which comprise half of our national territory), in oil and gas, in electricity, and in other types of activity." added Sarmiento. "We are beleaguered by a huge and inefficient bureaucracy, our education system is very poor, and 60% of our productive activity takes place in the informal economy. Our tax system is a nightmare."

Some analysts suggest there are other reasons why the privat sector is unhappy with the administration, including the perceived poor performance of Finance Secretary Luis Videgaray. "The business sector is angry with the Peña Nieto government, in particular with Luis Videgaray," columnist Leo Zuckermann wrote in the daily newspaper Excélsior. "He has been a disappointment."

Zuckermann said the private sector is justified in its dislike of Videgaray if his performance is measured on Mexico’s growth rate. "Last year he promised a growth rate close to 4%, and we ended at about 1.1%," said the columnist. "Earlier this year, he again projected growth of about 3.9%, but he has lowered his projection to about 2.7%. There is concern about an economy that continues to underperform."

Capital flight to Texas

Another huge problem facing Mexico is insecurity, which not only acts as a deterrent to foreign investment but has also led some Mexican companies to transfer a share of their operations to Texas.
A recent study by the Cámara de Empresarios Latinos en Houston (CELH) showed that millions of business owners from Tamaulipas and Nuevo León (primarily Monterrey) have set up shop in Houston and other communities in Texas since 2009 to escape criminal organizations. These businesses—which have been subject to extortion, threats, and other acts of violence from the Zetas and to a smaller extent the Gulf cartel in recent years—have sought a safe haven north of the border.

These business owners have opened hundreds of businesses in the Houston area, which has helped the economy of the city grow by about 35%, said CELH president Adriana González.

"They have moved here from Monterrey, from other parts of Nuevo León, from Tamaulipas, from the city of Tampico," said González, who noted that these immigrants are not only contributing to economic growth through their businesses but also as consumers.

González said that some 150 businesses have been opened in The Woodlands area of Houston alone in recent years. "These are all sorts of enterprises, from food to spas to medical establishments to restaurants of all kinds," said the CELH president.

Still, despite their strong presence in Texas, many of the business owners have not retired all their capital from their enterprises back home in Tamaulipas or Nuevo León. "The majority of their businesses back home have not closed, their operations here been opened as franchises," said González. She said some entrepreneurs who fled to Texas have already returned or are thinking of returning to Mexico even though they are keeping the operations they established in Houston and nearby communities.

-- End --