

Regional Economic Report

October – December 2013

Summary

Economic activity in all regions observed an expansion in the fourth quarter of 2013, although at a lower rate than in the previous one. The growth rate varied across regions. The economy of the Northern region registered greater dynamism, while the rest of regional economies presented signs of weaker growth in the reference quarter. With the exception of the Northern region, the indices of activity by region in the manufacturing, construction and agricultural sectors, as well as retail sales and hotel occupancy in most cases exhibited lower annual growth rates in the last quarter of 2013 as compared to the previous one.¹

By the end of the fourth quarter of 2013, annual headline inflation increased in all regional economies and located above the level registered in the previous months. This increment was mainly determined by two factors: first, unanticipated adjustments in public transport fares in some cities of Mexico and, second, higher prices of a reduced number of agricultural goods caused by climate shocks that had affected production over the previous months. In January 2014, as anticipated by Banco de México, annual headline inflation in all regional economies increased, consequent on adjustments in public prices and the fiscal measures that came in force at the beginning of the year. The referred increment was slightly more marked in the border cities of the Northern and Southern regions, due to the equalization of the VAT in the border region to the rate prevailing in the rest of the country. It should be pointed out that from the second fortnight of January onwards, annual headline inflation exhibited a downside trajectory, which was reinforced by inflation data of the first fortnight of February.

Business agents interviewed for this Report by Banco de México across all regions indicated, in general, that they expect demand for their goods and services to continue expanding over the next six and twelve months. This expectation is principally associated to greater recovery of domestic demand, particularly public investment in infrastructure, and to a moderate growth of external demand. It is noteworthy that some contacts were cautions regarding the expansion rate in the first half of the year. Likewise, in all regions the referred business contacts pointed out various risk factors that, if they happen to occur, could impact the expected growth rate of the respective entities. Among external risks, they mentioned the evolution of international environment, in particular, the possibility of new volatility episodes in international financial markets. Among domestic risks, the following were stated: further deterioration in perceived public safety, a smaller than foreseen extent of structural reforms, and a greater than expected impact of fiscal measures on consumer purchasing power. Likewise,

in some regions business agents also expressed concern over the dynamism of public expenditure on infrastructure and the occurrence of adverse weather phenomena.

As regards inflation expectations, interviewed business agents stated that they do not anticipate inflationary pressures on salary costs over the next six and twelve months, given the expected slack in regional labor markets. With respect to input prices, in general, lower annual growth rates are expected, even though business agents interviewed in the Northern and Southern regions anticipate an increment in these rates, as a result of the VAT equalization in the border region to the rate prevailing in the rest of the country. Still, the referred business contacts ruled out that the above could generate second round effects on the price formation process. Thus, in all regional economies, most business agents expect the annual growth rate of their sales prices to be lower than that of their inputs.

In 2013, the Congress approved a series of structural reforms aimed at invigorating the Mexican economy. Two Boxes are included in this Report, presenting an analysis, on the one hand, of the economic impact of these reforms as anticipated by business agents interviewed by Banco de México, and, on the other hand, of complementary deregulation measures at the local or state level, which could enhance the referred impact.

Box 1 discusses the opinion of business agents interviewed in early 2014 about the reforms approved in 2013, regarding two aspects: on the one hand, the degree of progress that, in general, is considered to have been made by means of approving these reforms, and, on the other hand, regarding those that are estimated to generate a greater impact on the economic activity in their entity in the medium term. With respect to the former aspect, and compared to the expectations prior to the reforms' approval, the interviewed business contacts generally showed a better perception of the achieved progress. With regard to the latter, in all regional economies, the energy reform was considered by most abovementioned agents as having the highest potential to boost regional economic growth.

Box 2 states that structural reforms – with the appropriate secondary legislation backing them and the adequate implementation – will be even more effective insofar as they occur in an environment facilitating new business start-ups. Thus, the study of interregional differences in the costs of business start-ups, presented in the Box “Regional and Municipal Indicators of Ease of Starting up New Businesses in Mexico” in the Regional Economic Report April-June 2012, is resumed. This time, the goal is to analyze some determinants of these differences. More precisely, the relation between the set-up costs and the deregulation of business start-up procedures is studied by federative entity. It is found that the implementation of measures to ease start-up procedures could significantly contribute to reducing costs of setting-up new businesses in Mexico.

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.