Overview

Mexico’s GDP grew by 1.5% YoY in Q4 2017, the slowest pace since the fourth quarter of 2013. On a quarter-over-quarter basis (compared to Q3 2017), Mexico’s GDP increased by 0.8%.

Consumption grew 2.1% YoY in Q4 2017, a deceleration from the previous quarter. The deceleration in household consumption could be explained in part by the high inflation that hit real wages in 2017.

Investment in Mexico continued on its negative trajectory. During Q4 2017, Gross Fixed Capital Formation (GFCF) contracted 2.5% YoY. This could have been driven in part by higher interest rates and the continued high uncertainties related to the renegotiation of NAFTA.

During 2017, inflation in Mexico was affected by internal and external factors that caused it to reach high levels. Recent data show that inflation has begun to subside. In March, CPI decelerated to 5.0% YoY, demonstrating that the price shock from the lifting of fuel subsidies has begun to ebb.

The Central Bank decided to keep the interest rate unchanged (7.5%) at its last meeting in April. The Central Bank highlighted the decrease in inflation in comparison to December and the anchoring of inflation expectations for 2018 as some of the reasons behind the decision.

It is expected that Mexican GDP growth could accelerate slightly in 2018. A contributing factor to this could be the continued strong US demand that will impact exports positively. Additionally, investment in the energy sector is expected to increase as a result of the recently implemented energy reform. A tighter monetary policy could cause inflation to continue to subside throughout 2018.
1. GDP

Mexico’s GDP grew by 1.5% YoY in Q4 2017, the slowest pace since the fourth quarter of 2013 (Figure 1). On a quarter-over-quarter basis (compared to Q3 2017), Mexico’s GDP increased by 0.8%.

The slowest pace of Mexico’s GDP growth was driven by a slowdown of household consumption and a lackluster investment (Figure 2).

Consumption grew 2.1% YoY in Q4 2017, a deceleration from the previous quarter (Figure 3).

The deceleration in household consumption could be explained in part by the high inflation that hit real wages in 2017. However, the strengthening of the labor market provided a positive countereffect; unemployment was at its lowest level since 2008 (Figure 4).
Investment

Investment in Mexico continued on its negative trajectory. During Q4 2017, Gross Fixed Capital Formation (GFCF) contracted 2.5% YoY (Figure 5). Investment in construction continues to decrease, and investment in machinery and equipment reported a contraction in Q4 2017 for the first time since Q4 2013. This could have been driven in part by higher interest rates and the continued high uncertainties related to the renegotiation of NAFTA.

Foreign direct investment (FDI) inflows decreased marginally in 2017 (-0.2% YoY) (Figure 6). Although the rest of the world FDI decreased 16.1% YoY, the FDI from the US increased 27.3%. The manufacturing sector attracted 45.3% of total FDI in 2017, but total FDI to this sector decreased 22.3% in comparison to 2016.


**Exports and Imports**

Exports experienced a favorable performance throughout 2017. During Q4 2017, exports increased 10.0% YoY (Figure 7). This expansion was mainly driven by manufacturing exports that have experienced steady growth throughout 2017. This is in line with the improvement of global economic activity and a weaker Mexican peso.

Imports also increased throughout 2017. During Q4 2017, imports registered a 10.8% YoY increase (Figure 8). The increase in imports of intermediate goods is consistent with the increase in manufacturing exports. Imports of capital goods were lackluster throughout 2017, being in line with the weak investment performance in 2017.

**2. Inflation and Monetary Policy**

During 2017, inflation in Mexico was affected by internal and external factors that caused it to reach high levels. In December 2017, Consumer Price Index (CPI) reached 6.8% YoY, the highest rate since May 2001 (Figure 9).

There are three main factors that affected inflation during 2017: 1) the increase in fuel prices due to the process of liberalization as part of the energy reform implemented by the government, 2) the depreciation of the Mexican Peso, and 3) the increase in the minimun wage that

---

**Figure 7: Exports of Goods**

% nominal change, YoY (SA)

Source: Bank of Mexico (Central Bank of Mexico), DataStream, MUFG

**Figure 8: Import of Goods**

% nominal change, YoY (SA)

Source: Bank of Mexico, DataStream, MUFG

**Figure 9: Inflation**

% YoY

Note: The number in the bracket is the weight on overall inflation (2010).

Source: INEGI, MUFG
entered into effect in December 2017 instead of January 2018 put more pressure on inflation during the last month of 2017.

Recent data show that inflation has begun to subside. In March, CPI decelerated to 5.0% YoY, demonstrating that the price shock from the lifting of fuel subsidies has begun to ebb.

The Central Bank decided to keep the interest rate unchanged (7.5%) at its last meeting in April. The Central Bank highlighted the decrease in inflation in comparison to December and the anchoring of inflation expectations for 2018 as some of the reasons behind the decision.

3. Exchange rate

The Mexican peso has been volatile. After regaining some of its lost value at the end of 2017, the Mexican peso experienced depreciation and has maintained its value since then (18.9 Mexican Peso per USD\(^1\)) (Figure 10). This depreciation could have been caused by the normalization process of the interest rate in the US, the uncertainty coming from the NAFTA renegotiation, and, to a certain extent, the electoral process.

4. Outlook

It is expected that Mexican GDP growth could accelerate slightly in 2018. A contributing factor to this could be the continued strong US demand that will impact exports positively. Additionally, investment in the energy sector is expected to increase as a result of the recently implemented energy reform. A tighter monetary policy could cause inflation to continue to subside throughout 2018.

---

\(^1\) As of the average of March 2018
For reference to our previous reports, see our website at: https://mufgamericas.com/economic-research

The information herein is provided for information purposes only, and is not to be used or considered as an offer or the solicitation of an offer to sell or to buy or subscribe for securities or other financial instruments. Neither this nor any other communication prepared by MUFG Bank, Ltd. (collectively with its various offices and affiliates, "MUFG Bank") is or should be construed as investment advice, a recommendation to enter into a particular transaction or pursue a particular strategy, or any statement as to the likelihood that a particular transaction or strategy will be effective in light of your business objectives or operations. Before entering into any particular transaction, you are advised to obtain such independent financial, legal, accounting and other advice as may be appropriate under the circumstances. In any event, any decision to enter into a transaction will be yours alone, not based on information prepared or provided by MUFG Bank. MUFG Bank hereby disclaims any responsibility to you concerning the characterization or identification of terms, conditions, and legal or accounting or other issues or risks that may arise in connection with any particular transaction or business strategy. While MUFG Bank believes that any relevant factual statements herein and any assumptions on which information herein are based, are in each case accurate, MUFG Bank makes no representation or warranty regarding such accuracy and shall not be responsible for any inaccuracy in such statements or assumptions. Note that MUFG Bank may have issued, and may in the future issue, other reports that are inconsistent with or that reach conclusions different from the information set forth herein. Such other reports, if any, reflect the different assumptions, views and/or analytical methods of the analysts who prepared them, and MUFG Bank is under no obligation to ensure that such other reports are brought to your attention. MUFG Bank, Ltd. retains copyright to this report and no part of this report may be reproduced or re-distributed without the written permission of MUFG Bank, Ltd. MUFG Bank, Ltd. expressly prohibits the re-distribution of this report to Retail Customers, via the internet or otherwise and MUFG Bank, Ltd., its subsidiaries or affiliates accept no liability whatsoever to any third parties resulting from such re-distribution.