



## **Economic update**

Mexico's Central Bank (Banxico) announced that it will keep rates at 3 per cent, in light of continued "weakness" in the economy and reduced pressure on inflation due to lower durable goods, telecommunications and energy prices. Furthermore, Banxico pointed out that a potential risk for inflation expectations in Mexico depends significantly on future moves by the Fed that could increase volatility in the peso's exchange rate with the dollar, however it expects inflation to stay close to, if not below, 3 per cent in 2015.

In line with Banxico's statement, the coinciding index (which attempts to measure the overall state of the economy) published monthly by the National Institute of Statistics and Geography remained flat, whilst the forward-looking index (which attempts to anticipate moves in the coinciding index) fell 0.08 points, its eight consecutive decrease.

Moreover, the indicator for private consumption fell during March by 0.3 per cent month on month. This is particularly discouraging, given that consumption had been the most dynamic driver in the Mexican economy during the past few months.

Yet on a more positive note, fixed investment bounced back in March after a nasty fall in February, growing by 4 per cent month on month and by 5.3 per cent year on year. The strongest growth came from investment in equipment, which grew by 3.2 per cent compared to the previous month, followed by construction, which grew by 3.7 per cent.

Thus notwithstanding the currently disappointing performance of the Mexican economy, investment both domestically and from abroad (which reached historic levels during the first four months of 2015) continue to be bullish about the country's prospects in light of its fundamentals and what might come from a series of ambitious structural reforms.

## **Risks in Mexico's mid-term elections**

This Sunday Mexico will head to the polls for mid-term elections. Whatever the outcome might be, on June 8<sup>th</sup> there will be a renewed Chamber of Deputies (Lower House of Congress), nine new governors, 16 new heads of Mexico's City's

*delegaciones* (boroughs) as well as new mayors across 993 municipalities and local congresses in 16 states.

The final outcome in terms of the Chamber of Deputies will determine the fate of future budget negotiations and pending pieces of legislation, i.e. the political status of Mexico City, President Peña Nieto's "security Decalogue", a new transparency law, among others. Despite the President's low approval ratings (in the order of 32 per cent) the latest preference polls suggest that the PRI has a decent chance of winning a majority in the Chamber of Deputies –albeit only thanks to its alliance with the Green Party and Partido Nueva Alianza. The PAN will almost definitely come in second. The second big question is to what degree will left-wing party PRD manage to stave off the advance of its offshoot Morena, a new party led by former mayor of Mexico City Andres Manuel Lopez Obrador.

Out of the nine states that will elect their new governor, only Campeche –where the PRI will win- has a clear outcome. The remaining eight states are too close to call. However, the contest that will be in the spotlight is that of the state of Nuevo León, given that it might be the first time that an independent candidate wins a governorship, in the form of Jaime Rodriguez "El Bronco" (the stallion).

An independent victory in Nuevo Leon would act as an experiment to how (if not whether) such political actors can govern without having a party behind them, which in turn will determine the emergence of a strong independent candidate in the 2018 presidential elections. Regardless of whether he wins or not, his strong performance during the campaign as well as those of a handful of other independent candidates across the country has added a new, even if thin, layer of incentives for political parties to behave.

One serious point of concern is that these have arguably been one if not the most violent elections in Mexico's history. Though focused in certain states, the execution of 21 people involved in the campaigns including various candidates and spanning across parties is a reminder not only of the pending challenge to curb violence in the country, but of the type of pushback to be expected in the process by criminal organizations who actively try to shape local politics.

Yet perhaps the most serious risk to have emerged from the elections was the government's U-turn on teachers' assessments, which is one of the fundamental changes to have come through thanks to the 2013 education reform –one of eleven structural reforms, which catapulted President Enrique Peña Nieto's international reputation. Although the education reform was somewhat overshadowed by those such as related to the energy sector or economic competition, it is certainly the most important one for Mexico's long-term growth, particularly given the country's abysmal performance in international competency tests.

The decision was made after repeated threats by one of Mexico's two national teachers union, the CNTE (as known by its Spanish acronym) that they would sabotage the electoral process in states such as Guerrero and Oaxaca, unless the assessment were cancelled.

The move renews much-touted doubts on the government's capability to implement the reforms. Though there is still a chance that President Peña Nieto might be waiting to see with how strong a mandate he comes out with on June 8<sup>th</sup> in order to throw his weight against the CNTE.