U.S.–MEX: ECONOMY

When the U.S. Catches a Cold…

by Héctor Rangel Domene

Mexico and the United States have a lot in common, but the two countries also have many differences that need to be taken into consideration if we are to improve our relationship and forge a brighter future.

The North American Free Trade Agreement (Nafta) has made our economies more intertwined than ever before. Mexico is the United States' third largest trading partner, as evidenced by the fact that according to figures released by the Banco de México, 82 percent of Mexico's exports go to the U.S. and more than 50 percent of Mexico's imports come from the U.S. Remittances also form a critical connection between the two nations: Mexico received $24 billion in remittances in 2007, most of which came from the approximately 5.7 million Mexican immigrants living in the United States and sending funds to their families back home. On the tourism front, about 85 percent of Mexico's visitors come from the U.S. and Canada.

Commodities are another important source of trade. The majority of Mexico's oil exports are destined for the U.S. market. In turn, Mexico imports approximately 12 million tons of grain annually from its northern neighbor. Mexico's financial and capital markets are also completely globalized and linked closely to the dollar. The country now has more than $90 billion U.S. dollars in reserve — an historic high.

Unfortunately drugs and arms also have become part of the cross-border traffic. Whatever we do or fail to do to stem these flows will have a tremendous bearing on our common future. Drug cartels and criminal organizations regularly purchase arms in the U.S. — not just handguns but automatic machine guns, grenades and rocket-propelled grenades — and smuggle them into Mexico. According to official statistics from the Mexican government, between January 2007 and March 2008 an estimated 14,000 weapons were sized from the drug cartels — most of which entered the country from the U.S. — enough to equip a small army.

In light of these facts, where is the Mexican economy? A quick review of the year 2007 tells us that gross domestic product (GDP) growth was 3.2 percent with fiscal balance. Although consumer prices rose 3.8 percent, Mexico's public debt was less than 26 percent of GDP, and the commercial trade deficit was small. The country could also boast of a well-capitalized financial system, which experienced 26 percent growth in banking credit in real terms last year. In terms of absolute numbers, in 2007 foreign direct investment totaled $23.2 billion, and GDP was close to $1 trillion. These figures make Mexico the 13th largest economy in the world. However, income disparity is still a problem: despite important advances over the last decade, over 40 percent of

Foreclosure bus tours in San Diego, California.

Photo by Cory Doctorow.

Mexico's population continues to live in poverty.

Originally, estimates for 2008 predicted that growth would be just under 3 percent, with inflation hovering around 4 percent. However, the recent crash of the U.S. housing market and losses in the U.S. financial system combined with supply and demand shocks in the commodities markets have caused us to reexamine these figures. The debate is now centered on how deep the economic downturn will be and how long it will last. Obviously, due to the close economic ties between the two countries, a recession in the U.S. will mean a slowdown for Mexico. It is still very difficult to estimate how severely the Mexican economy will be affected; inevitably, there will be a strong impact. Analysts are now estimating that U.S. GDP will grow by only 1 percent this year, in which case Mexico will probably grow a little over 2 percent.

On the bright side, Mexico's economy is stronger than ever, a fact which should help mitigate the effects of a U.S. recession. There are a number of elements that contribute to this strength. First of all, the price of Mexican oil is nearing $100 a barrel and continues to rise, leading to high dollar revenues for the country despite the downward trend in export volumes. While the growth of remittances has slowed, they remain at historically high levels. The economy is stable and inflation is low due to fiscal and monetary discipline on the part of financial authorities. Foreign exchange reserves are high, and the weak U.S. dollar has encouraged Mexican exports to Europe in recent months. With exports up, the demand for intermediate goods and raw materials is also high.

On the domestic front, conservative financing policies have enabled the Mexican housing market to soar: government-sponsored mortgages between 2002 and 2007 reached 2.2 million, nearly equaling the total for the previous 30 years, 2.1 million. European tourists continue to flock to the nation's beaches and historic sites. An ambitious infrastructure investment program has been announced by the Mexican government that will amount to more than $40 billion over the next five years. In addition, the Calderón administration is paving the way for higher and more stable growth rates by taking on the structural reform agenda. Two recently approved reforms, of the fiscal and pension systems, will strengthen the economic and political environment, especially if they are combined with energy sector reform, which is currently under discussion in Congress.


Photo by Ben Smith.

Resorts in Cancún, Mexico.

Another factor which has built confidence in Mexico's political leadership is the high priority President Calderón has placed on fighting organized crime and the drug cartels.

Looking to the future in this election year, Mexicans are hoping for a U.S. president who can get the economy back on track. The U.S. economy is 25 times as large as Mexico's, and even though both are highly integrated, the well-known saying "When the U.S. catches a cold, Mexico ends up with pneumonia," might not hold true this time. With structural reforms in place, no domestic imbalances and stronger internal demand, perhaps the popular saying should be rephrased as "When the U.S. catches a cold, Mexico ends up with a cold as well." There is also the hope in Mexico that the U.S. will follow the European Union model and invest heavily in its southern neighbor. Europeans channeled resources to less-developed member countries like Spain and Ireland, and the economic and political transformation has been enormous. A similar degree of U.S. investment in Mexico would help guarantee a more prosperous and secure region, an outcome which is undoubtedly in the interest of both partners.

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