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Mexican Housing: Public Policies Contributing to its Competitiveness and Growth

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Vivir Mejor

- 1) Economic Perspectives for 2009
- 2) Public Policies Facing the Recession and their Impact on the Housing Sector
 - a) October 2008 Agenda
 - b) January 2009 Agenda
- 3) Concluding Remarks

Economic Perspectives for 2009



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- Global economic performance forecasts continue to be revised downward. In general, analysts have constantly revised their 2009 growth forecast. The most salient revisions took place during the third week of November 2008.

World 2009 Growth Forecasts
(Annual variation, %)

	FMI	Blue Chip	Prom. Corr.	Bloomberg	
	January 28	January 10	January 28	January 22	Standard deviation
United States	-1.6	-1.6	-1.9	-1.5	1.3
Japan	-2.6	-1.4	-3.8	-2.0	1.6
United Kingdom	-2.8	-1.8	-2.5	-2.2	0.5
Euro Zone	-2	-1.2	-1.9	-1.8	0.7
Russia	-0.7		0	-0.8	2.0
China	6.7	7.1	7.8	7.7	1.2
Brazil	1.8	2.1	1.5	2.9 ²	0.5
Chile			1	2.9 ²	0.9
Mexico	-0.3	-0.1	-0.1 ¹	0.8 ²	0.7
World	0.5		0.2		

For Mexico in 2009:

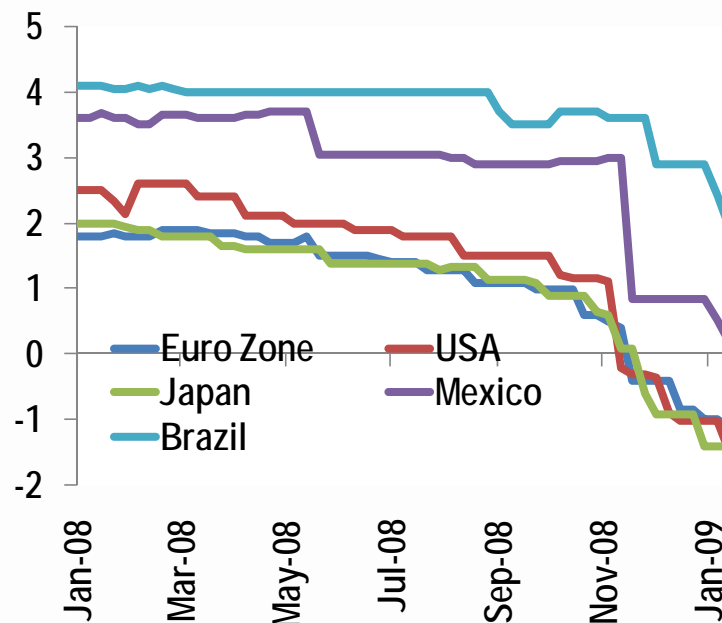
Bank of Mexico: -0.8% - -1.8%

Ministry of Finance 0%

1/ Mexican Private Sector Survey.

2/ November 21 2008

Evolution of 2009 Growth Forecasts
(Annual variation, %)



Source: Bloomberg/Blue Chip

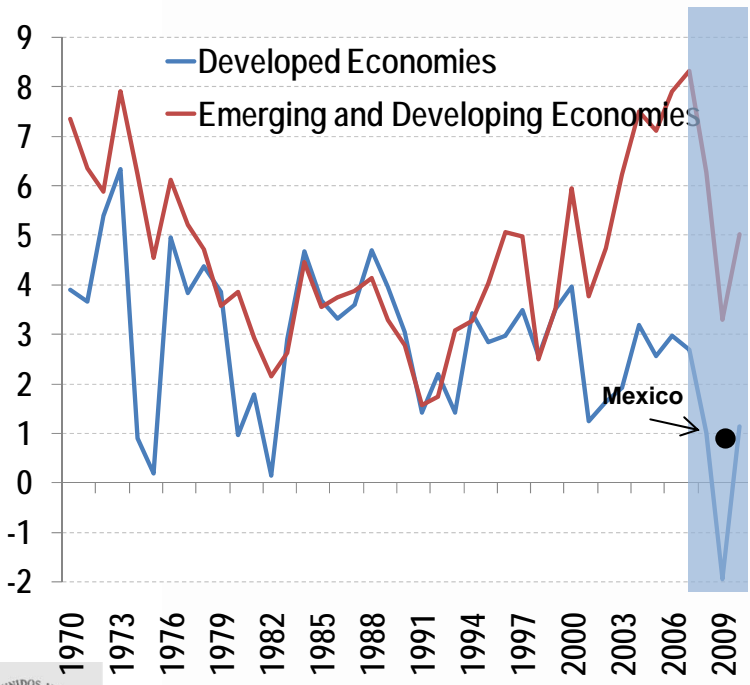




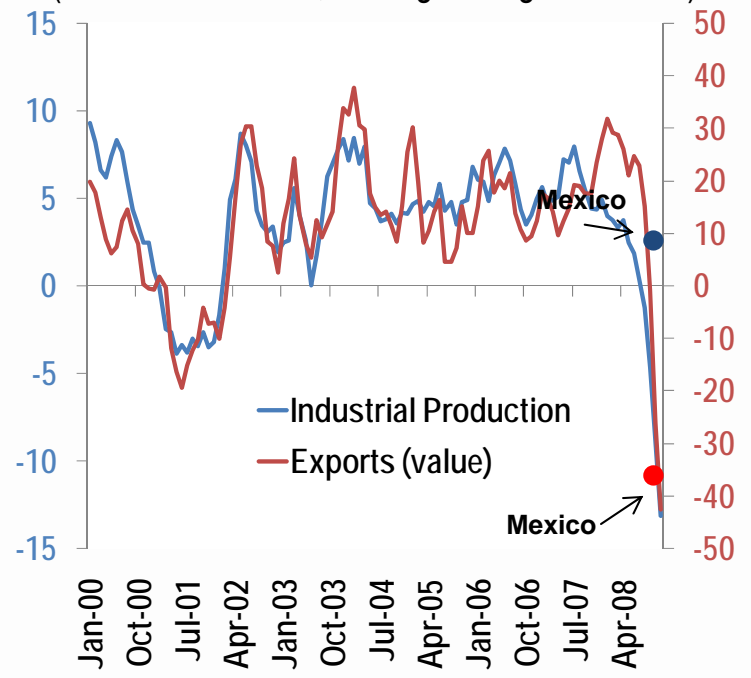
Economic Perspectives for 2009

- Despite the measures adopted to heal the global financial system, credit restrictions have directly affected the real economy.
- Financial uncertainty has driven firms and families to reduce their spending and contract their production and global commerce.

Global GDP Annual % Growth



Global Industrial Production and Exports Growth (Annual % variation, moving average 3 months)



Source: IMF



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Public Policies Facing the Recession: October 2008 Agenda



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- Program to Stimulate Growth and Employment (October 2008):
 - 1) Increase public spending in infrastructure (by close to 50 billion pesos)
 - 2) Speed up public spending in infrastructure, though a simplification of related regulation
 - 3) Construct a new oil refinery for Pemex
 - 4) Give an extraordinary impulse to small and medium enterprises (give credit by 165 billion pesos)
 - 5) Accelerate tariff reduction and deregulation
- This last measure consisted of a comprehensive trade liberalization initiative, aimed at furthering Mexico's integration into the world market, improving the competitiveness of its economy, and reducing domestic market distortions.



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Protectionist pressures on trade



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- In the context of an economic slowdown, governments tend to face increased pressure to establish trade protectionist policies.
- Different countries have decided to respond to the current crisis and the corresponding protectionist pressure in different ways.
- In the case of Mexico:
 - We have used every opportunity to reinforce our commitment to an open economy.
 - We have chosen to go ahead in implementing our trade liberalization initiative.
- A key element for the adoption of this liberalization initiative was the development of an active dialogue strategy with all actors involved, and the commitment of the Mexican government to work on several aspects hindering competitiveness of the Mexican industrial sector.

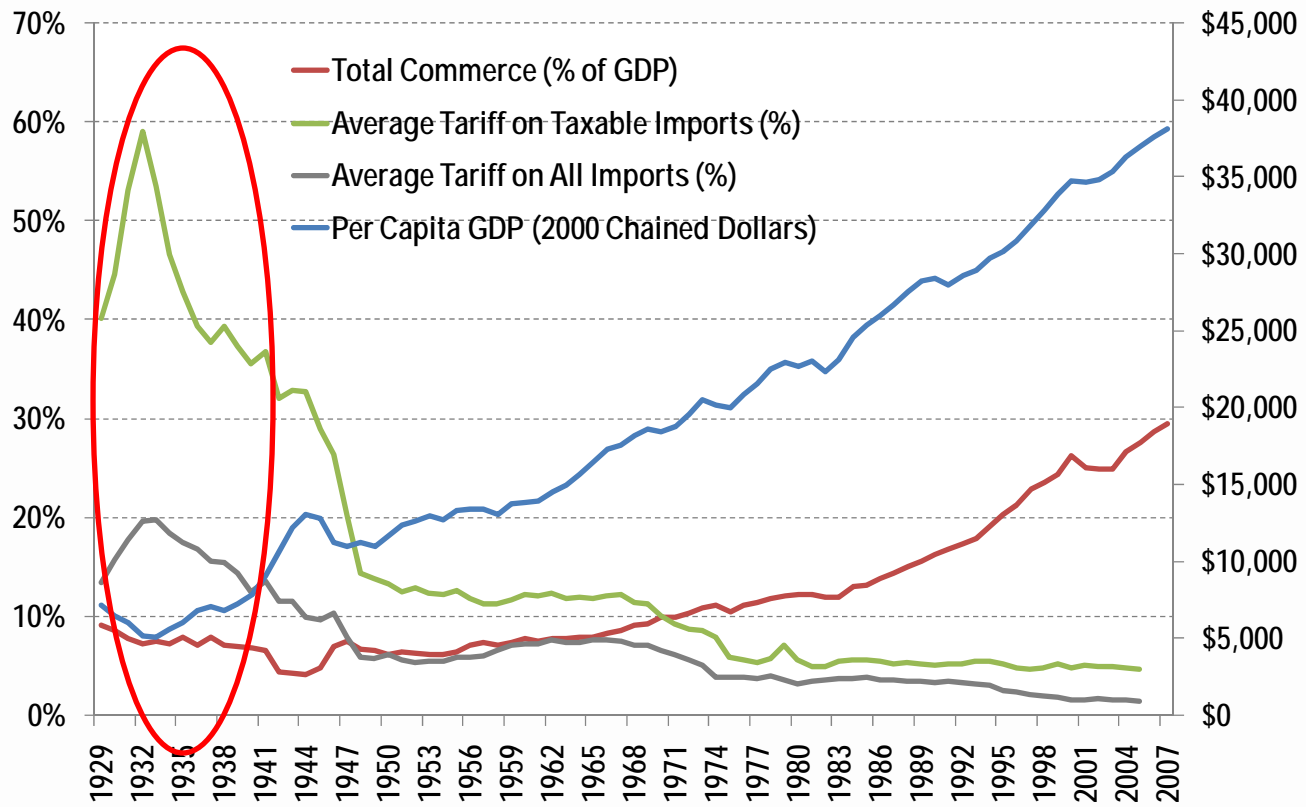


Protectionist pressures on trade: historical evidence



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- The experience of the Smoot-Hawley Tariff Act, published at the beginning of the 1929 Great Depression, illustrates the dangers of adopting trade barriers in response to a financial crisis. Economic historians agree that the depression was deeper and the recovery slower as a result of this and other protectionist measures adopted.



Trade liberalization: motivation



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- The trade liberalization initiative implemented in Mexico in December 2008 responded to the following motivation:
 - Mexico's main comparative advantage is its geographical location in relation to the US market. However, the dynamism of other economies deteriorated Mexico's position in recent years.
 - Mexico needs to improve its position with respect to high growth economies with which there is no FTA.
 - Mexico's insertion into the world economy stagnated during the last decade.



Trade liberalization: motivation



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- Among the elements identified as obstacles to Mexico's competitiveness are restrictions to international trade.
 - The most recent version of the Global Competitiveness Index of the World Economic Forum ranked Mexico among 134 countries in the following positions:
 - 60 in the general ranking
 - 105 in the average tariff ranking
 - The Doing Business 2009 study published by the World Bank ranked Mexico among 178 countries in the following positions:
 - 56 in the general ranking
 - 87 in the foreign trade efficiency rating



Trade liberalization: motivation



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- Mexico has signed free-trade agreements (FTAs) with countries that have, on average, a lower growth rate than other developing economies with which there is no FTA. This can limit Mexico's economic growth potential.

FTA		Non-FTA	
Region	Weighted Average Growth Rate	Country	Actual Growth Rate
United States, Canada	1.31%	China	10.22%
Costa Rica		Cambodia	8.00%
Venezuela, Colombia		Vietnam	7.62%
Bolivia		Singapore	6.48%
Nicaragua		India	6.37%
Chile		Malaysia	6.19%
European Union		Korea	5.43%
Israel		Taiwan	5.28%
Salvador, Guatemala, Honduras		Bangladesh	5.24%
Norway, Iceland, Liechtenstein, Switzerland		Sri Lanka	5.10%
Uruguay		Thailand	4.71%
Japan		Hong Kong	4.30%

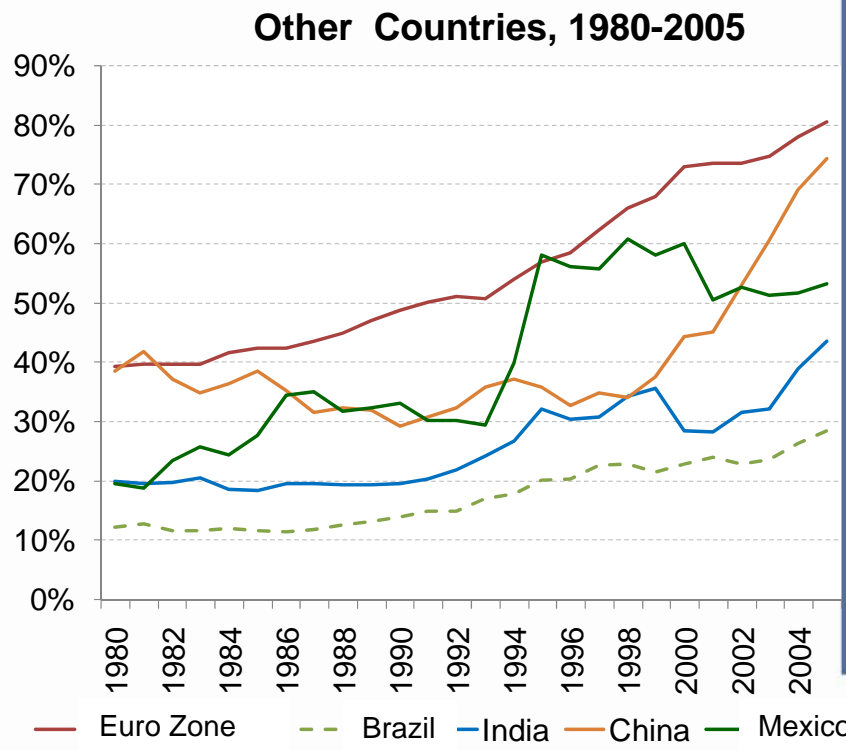
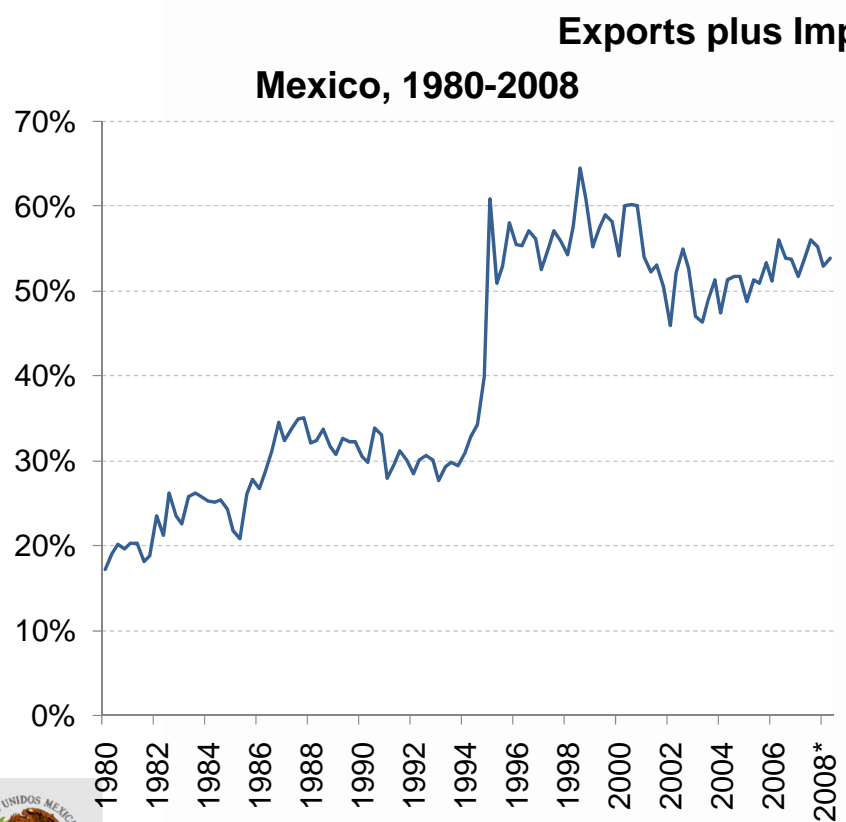


Trade liberalization: motivation



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- Since the mid-eighties, the Mexican economy experienced a process of trade liberalization which made it much more open to the world economy. However, during the last decade the participation of international trade in GDP stagnated at less than 60%.



Source: INEGI

Source: INEGI and World Development Indicators, World Bank



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Trade liberalization: motivation



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- Mexico's process of insertion into the world economy has taken place in three stages:
 - Unilateral liberalization (1985-1987)
 - Free trade agreements (1994 -)
 - Special programs with tariff exceptions for certain sectors and firms (2001-2008)
- This process resulted in a tariff system characterized by a high level of complexity and by high costs.
- Out of all imports:
 - Only 9% paid the general tariff
 - 31% requires certificates of origin verification to access FTA benefits
 - 20% enters the country through special programs
- The complexity of the tariff system generated perverse incentives.



Trade liberalization: recent actions



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- In response to this situation, in December 2008 Mexico published a trade liberalization initiative that comprised the unilateral reduction of industrial tariffs in 5 annual cuts, with the following results:
 - The average tariff will go down from 10.4% in 2008 to 4.3% in 2013.
 - The tariff dispersion will go down from 9% in 2008 to 6.4% in 2013.
- This measure will promote trade with both non-FTA and FTA partners, in the latter case by making the use of certificates of origin redundant.

IMPORT TARIFF INDICATORS

	2008	2009	2010	2011	2012	2013
Average Tariff (%)	10.4	8.3	5.2	4.6	4.4	4.3
Tariff Dispersion (Standard Deviation)	9.0	8.1	8.0	7.3	6.6	6.4
Number of Tariff Lines at 0%	2,179	2,571	6,627	6,871	6,871	6,871
Percentage of Tariff Lines at 0%	20.1	23.6	60.9	63.1	63.1	63.1



Trade liberalization: recent actions



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- According to some analysts, this is the most ambitious trade liberalization program adopted by Mexico in the last 20 years.
- With this program, the average tariff in Mexico will reach a level similar to that of our main trade partner, the USA.
- Differences in tariffs will be maintained only for final consumption goods for which there is an important productive sector in Mexico and not in the USA.

TARIFF ADJUSTMENTS PUBLISHED IN DECEMBER 2008

Type of Goods	Tariffs		
	USA	Mexico	
		2008	2013
Consumption goods	5.9	21.8	13.3
Intermediate goods	3.2	8.5	2.5
Capital goods	1.7	9.3	4.4
Total	3.8	10.4	4.3



Trade liberalization: impact on the housing sector



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- The housing sector will benefit from the trade liberalization program through the reduction of tariffs on some materials that have an important participation in construction costs.

IMPACT OF TARIFF REDUCTION ON CONSTRUCTION COSTS

Sector	% of total costs	Tariff reduction ^{/1}
Non-metal mineral products	20.0	6.5
Basic metal industries	16.6	6.8
Plastic and rubber industries	6.3	5.6
Metal products	6.2	6.5
Chemical industry	2.6	4.3
Electric equipment and accesories	2.5	6.4
Lumber industry	1.9	6.2
Machinery and equipment	1.2	3.8
By-products of oil and coal	1.0	4.5
Furniture and related products	0.4	5.4
Paper industry	0.2	5.9
Textile products, except clothing	0.1	11.5
Transport equipment	0.1	7.8
Computers, communication, measurement and electronic equip. and electronic accesories	0.1	4.2
Total / weighted average^{/2}	59.2	3.7

^{/1} Tariff reduction from 2008 level to 2013 level, percentage points

^{/2} Average tariff reduction for construction materials weighted by the % of total construction costs, percentage points

Source: Ministry of Economy calculations using data from INEGI



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Trade liberalization: impact on the housing sector



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- Furthermore, the markets for some inputs that have been very concentrated will face increased competition, generating additional downward pressure on prices.

Industry	Number of firms		Aggregate Value				Concentration Index	
			(Billions, 2002)		4 largest firms (% of total)			
			MEX	USA	MEX	USA	MEX	USA
Chemical industry	3,073	9,659	11.7	256.2	51.0	15.7	271	126
Basic iron and steel industry	20	302	0.5	18.8	97.2	44.2	901	650

Source: INEGI for Mexico and U.S. Census Bureau for USA



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Public Policies Facing the Recession: January 2009 Agenda



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- Agreement in Favor of the Economy and Employment (January 2009):
 - 1) Support to employment and workers
 - 2) Support to Mexican families' economy
 - 3) Support to competitiveness and small and medium enterprises
 - 4) Investment in infrastructure
 - 5) Efficient, timely and transparent public spending
- Among the measures comprised by the first pillar is the Program to Preserve Employment, which will be implemented by the Ministry of Economy.



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Program to Preserve Employment



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- The Program to Preserve Employment was created as part of the package of measures announced on January 7 by President Calderón.
- The goal of the Program is to protect employment and specific human capital in those industries most vulnerable to foreign demand fluctuations and that have been the most affected by the world economic slowdown.
- This will be achieved by motivating the use of practices that reduce labor costs for firms by reducing work time and salaries, instead of implementing lay offs.



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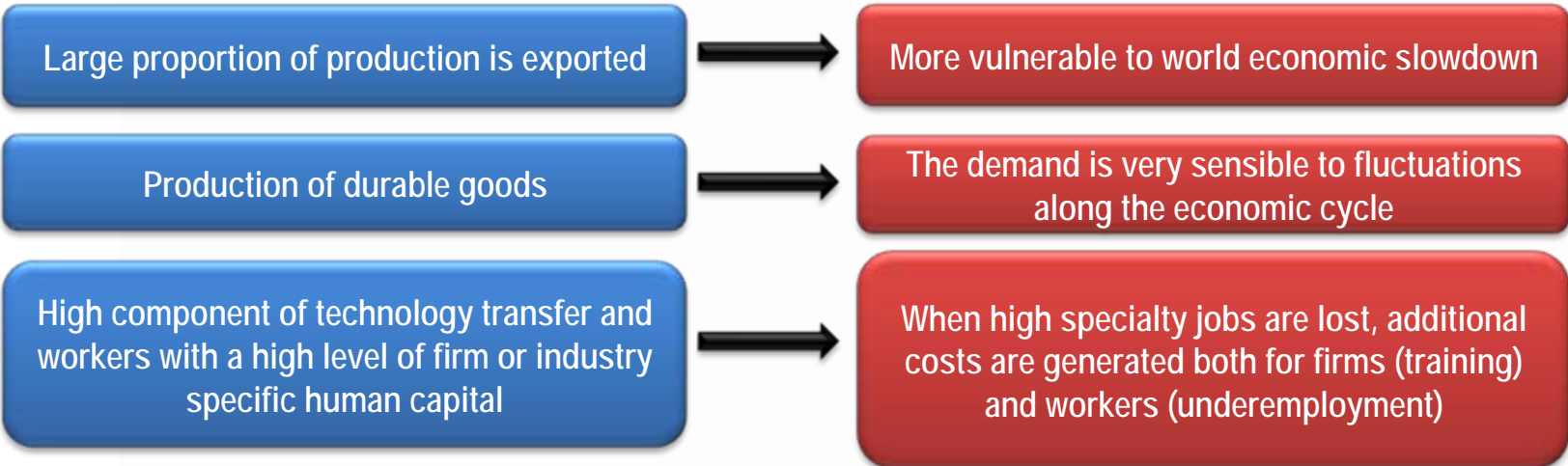
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Motivation and benefits

- The Program is targeted at sectors that are more vulnerable to the adverse economic environment because they have a strong orientation towards foreign trade and towards the production of goods for which consumers can easily defer demand.



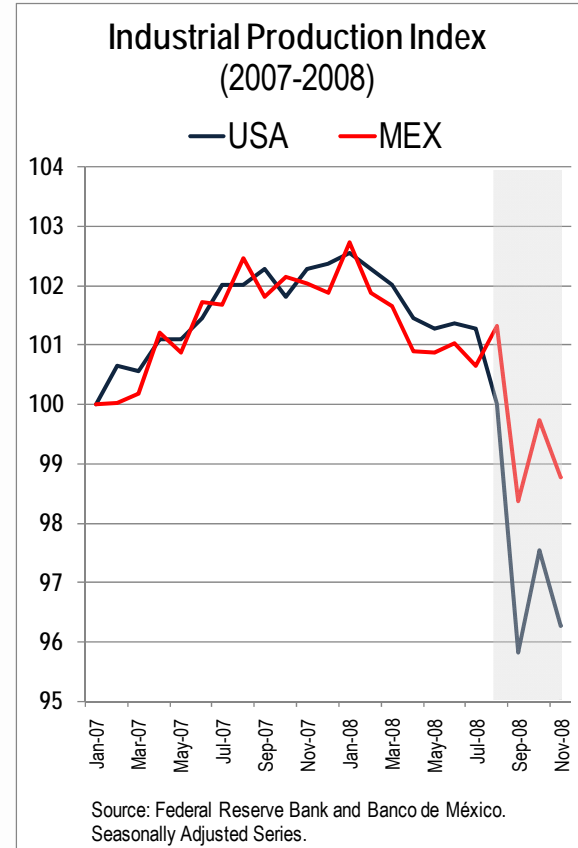
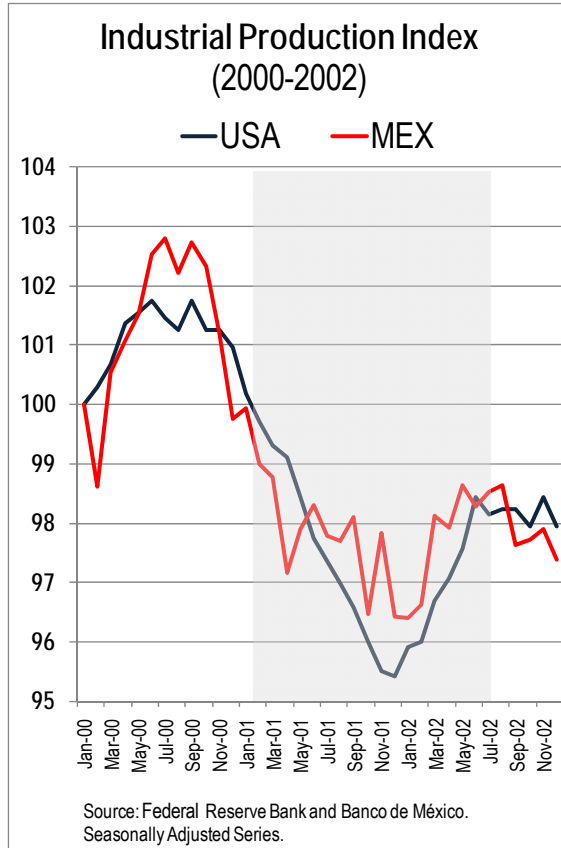
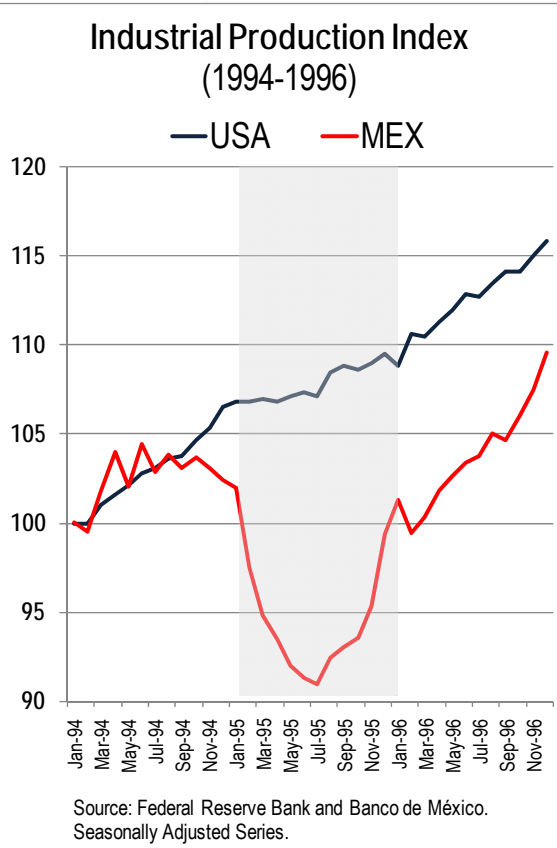
- Firms receiving support will be those in the following sectors: Fabrication, assembly and repair of electric, non electric, electronic and transport equipment and machinery, as well as auto-parts.

Current and previous economic slowdowns



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- While economic crisis in Mexico during the eighties and nineties were generated by internal unbalances, the current and the 2001 slowdowns were both triggered by reductions in external demand.



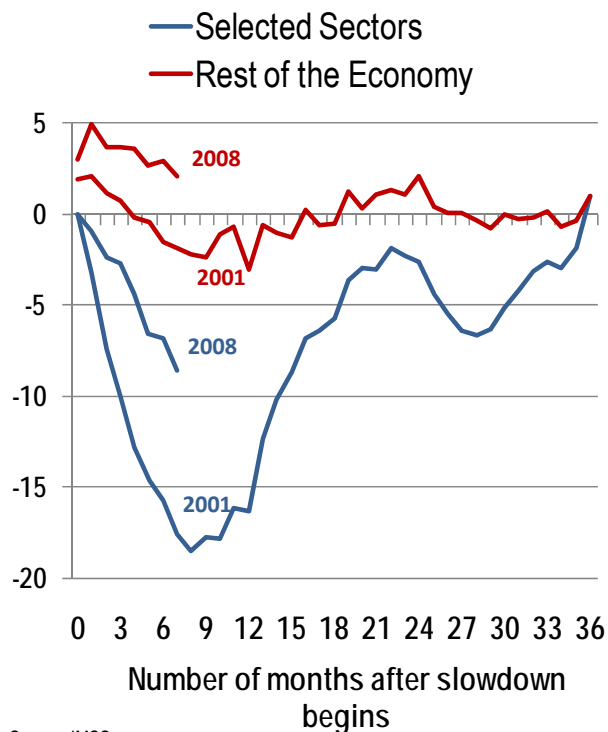
Selected sectors characteristics



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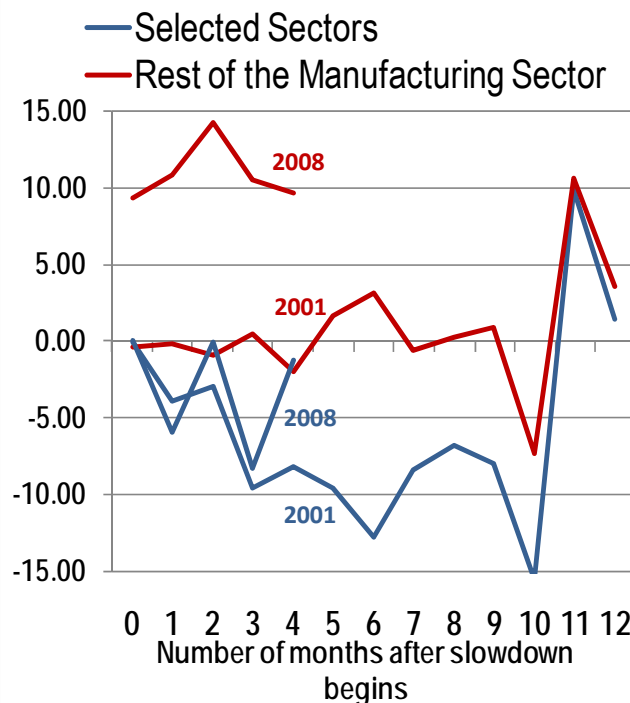
- Employment and production in sectors selected as beneficiaries of the Program to Preserve Employment are more sensitive to slowdowns in comparison to the rest of the economy.

Evolution of Employment (Year to year % change)



Source: IMSS
Data until November 2008.
*/ Slowdown starts when the yearly change in number of employees is 0% and negative for the consecutive periods (March 2001 and March 2008).

Evolution of Production (Year to year % change)



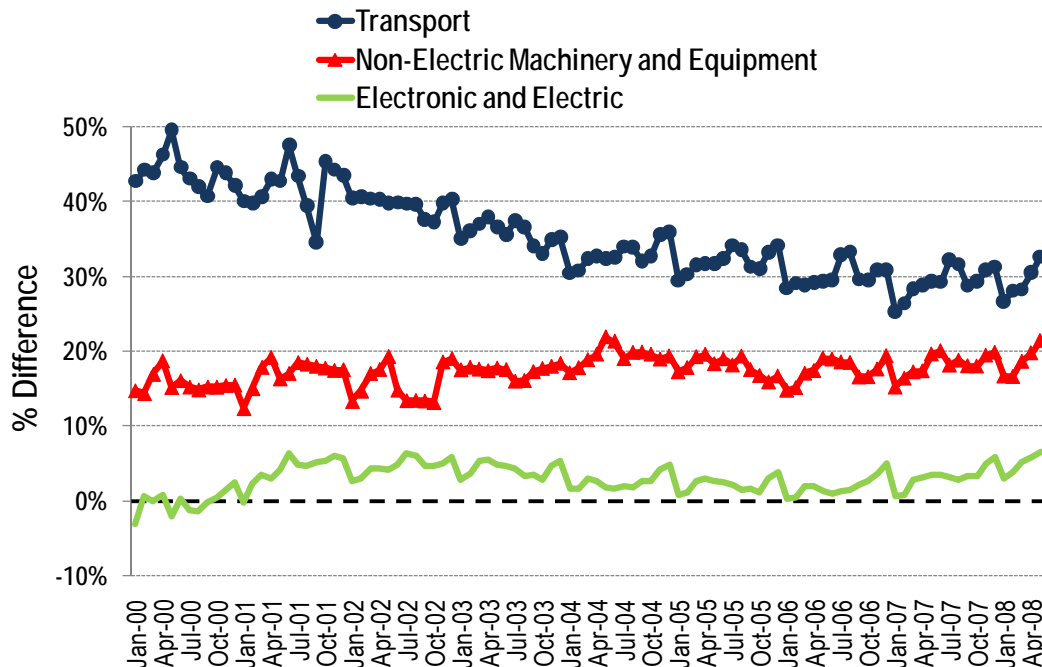
Source: Monthly Industrial Survey from INEGI
Data until September 2008.
*/ Slowdown starts when the annual growth of production is 0% for selected sectors and negative for the consecutive periods (May 2001 and May 2008).



Human capital protection

- Workers in these sectors own a high level of specific knowledge and abilities, a condition that is reflected in the wage differential.
- Under the current uncertainty of economic perspectives, this Program will encourage firms to preserve human capital by reducing their payroll cost.
- In addition, the Program will help to ease the recovery process.

Difference between selected sectors' wages and general wage (%)



Source: CONASAMI

Program to Preserve Employment: impact on the housing sector



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- The Program's positive impact on the housing sector is twofold:
 - First, less unemployment implies less payments overdue in mortgages. This will contribute to maintain favorable financing conditions for construction and acquisition of houses.
 - Second, the common practice among Mexican firms and workers that convene a reduction in work time and salaries is to keep social security and INFONAVIT contributions unchanged. This situation increases certainty and helps workers to keep their long term investment plans, such as buying a house.



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Concluding Remarks

- The implementation of counter-cyclical public policies by the Federal Government will contribute to softening the impact of the global economic slowdown on the Mexican economy, by stimulating domestic demand and reducing uncertainty for consumers.
- While counter-cyclical policies have played an important role, they have not distracted the Federal Government's attention to the development of structural measures much needed to enhance the economy's competitiveness. It is worth noting the following structural measures:
 - Aggressive development of infrastructure
 - PEMEX Reform
 - Trade liberalization



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