Economic Analysis

How is investment in Mexico evolving?

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Recently, the data on gross fixed investment as of March was released. This indicator grew at a monthly rate of 0.5% and 8.8% compared to the same month of the previous year. Investment is essential to analyze the economy both because it is the component of aggregate demand that fluctuates the most - and therefore allows analysis of economic cycles - and secondly because it is the component that most affects long-term growth since it explains the evolution of the capital stock that, together with productivity, determine the potential growth rate of GDP per capita.

There was undoubtedly good growth in March, but it's worth asking how investing is doing from a broader perspective. With the publication of this new data, gross fixed investment is 2.1% below the level of January 2019, when this administration began. This fact is worrying because the fact that investment has not grown in more than four years will result in lower economic growth ahead. To my mind, two main factors explain this poor investment performance. First, some public policies have generated uncertainty among investors, leaving the impression that contracts are not necessarily respected and that the game rules can change arbitrarily after the investments have been made.

This has been the case above all in the energy sector. The second factor is that we have been in an environment of restrictive real interest rates for over a year. One of the most critical determinants of investment is the interest rate: the higher it is, the lower the investment companies make.

However, it is essential to point out that this weakness in investment began during the previous administration, first with a decrease in public investment and later because the presidential election in the United States in 2016 brought high uncertainty regarding the future of the Free Trade Agreement, resulting in a stagnation of private investment. Thus, total investment in the country has gone from 22.2% of GDP in 2012 to 19.1% (16.5% private and 2.6% public) at the end of 2022. Of the investment in Mexico, approximately 88 % is national, and 12% comes from abroad. For the country to increase potential growth to levels that make it possible to reduce poverty significantly, investment is required to be at least 25% of GDP. Countries like Singapore, Taiwan, and South Korea, which managed to go from emerging to developed economies in the last half-century, had more than 25% average investment rates for several decades.

An interesting pattern emerges if we analyze the investment behavior by component in recent years. As I already mentioned, total investment is 2.1% below the level at the beginning of this administration. But its components have had very different trajectories: while construction is 12.5% below the mentioned level, the acquisition of national machinery and equipment registered a rise of 6.5% and 16.4% in the case of imports, with a notable acceleration in the last two years.

I think this is a sign that nearshoring or relocation is beginning to have an effect in the country. But the fact that both construction (which includes the construction of new plants) and foreign direct investment -as I explained in my previous article- have not increased suggests that investors, foreign and national, who are already operating in the country and who know better navigate the current political environment, they are the ones who are most encouraged to invest (acquiring capital goods) and expand their production by making more intensive use of their existing plants.

In contrast, those who still do not have a presence in the country have doubts about doing so. To increase the level of investment in the country, these doubts must be dispelled: provide greater certainty by strengthening the rule of law.

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