Economic Analysis

Positive signs in fiscal policy

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Mexico's Ministry of Finance and Public Credit (SHCP) has recently issued indications that I view as positive and that have been well received by the markets. The most important of these concerns the recently announced preliminary criteria for economic policy.

It is welcome news that the Ministry of Finance has lowered its growth forecasts, both for this year (from an estimated 2% to 1.6%) and for the next (from 2.6% to 1.9%). By its timely acknowledgment that growth will be slower than expected when the fiscal package was put together for this year, the Finance Ministry is accepting that spending adjustments will be needed if the fiscal targets adopted in that package are to be met. This is not only because fiscal incomes will be lower than expected – public revenues slumped by 3.9% YoY in the first two months of the year – but because slower growth will mean lower Gross Domestic Product (GDP) and, as such, a lower surplus insofar as it is a proportion of that. For this reason, it is fortunate that the federal government is considering spending cuts. This means that it is prioritizing its target of 1% of GDP for the 2019 primary surplus. It is also worth noting that these cuts are to be applied on current expenditure, not investment, which could reduce the economy's growth capacity in the medium term.

Among other measures, 16 thousand jobs in Pemex may be slashed, which would improve the company's financial situation without affecting productivity in the slightest. Cuts have also been announced for next year that would trigger a real annual fall of 1%, with the aim of reaching a primary surplus of 1.3% of GDP. This aim seems to me to be even more ambitious than necessary in order to keep the trajectory of debt as a ratio of GDP stable, and to be well received by the markets. Although, in any event, it is leaving room for a margin of error, particularly because of possible fiscal contingencies that the status of Pemex might bring about, and also because the goal set for petroleum production of 1.92 million barrels a day appears optimistic.

This is a responsible course of behavior on the part of the Ministry of Finance and will prevent a deterioration of the country's fiscal position with the attendant macroeconomic instability. We should recall that six years ago, when the previous administration started governing, the situation was similar: growth began to be slower than expected (we should remember that overly optimistic forecasts had been presented) and there was no reaction; the reality of lower growth was not acknowledged, and spending was not reduced, a state of affairs that lasted for the first three years of the previous government. This caused debt as a proportion of GDP to rise by 15 points over that period – with no improvement to the country's infrastructure to offset it. This increase in debt has meant that the country has less room for fiscal maneuver, because it has to use more resources on servicing it. In addition, when spending corrections were finally made, due to the pressure from rating agencies, these adjustments focused on investment rather than current account spending, which reduced the country's growth potential.

Another positive sign in fiscal terms was given by Sub-secretary Arturo Herrera when he mentioned that the country had to collect more taxes from real estate and possessions. Although these taxes are local, it would be most helpful if the states followed Herrera's recommendations, recommendations that reveal a concern to strengthen tax collection. Both taxes are effective because collection is easier to enforce, they are progressive and in the case of possessions, they are environmentally sound. A progressive government that is interested in income distribution should be backing these kinds of taxes. We hope that fiscal policy continues to be led by the Ministry of Finance and Public Credit.

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