BBVA Research

Global Economy

Fiscal policy in Mexico: a challenge to be addressed

El País (Spain)

Carlos Serrano

Mexico is facing important fiscal challenges. On the one hand, its tax collection is very low: tax revenue as a share of the GDP (only 14%) is not only the lowest in the OECD, but it is also low when compared to other Latin American economies. On the other hand, the space to increase expenditures is very small. Although public debt as a percentage of GDP - currently at around 45%- does not seem particularly high, there is little room for expansion, as the debt servicing costs are very high.

In this context, the new Administration of President López Obrador has sent out positive signals in terms of his commitment to meet the primary budget surplus targets in order to stabilize public debt. Not only he presented a prudent budget based on credible assumptions, but when it became evident that the economy would grow less than expected, this was met with spending cutbacks to ensure that budget goals were complied with.

However, these spending cuts, in conjunction with the reallocation of expenditure items, where spending has been steered towards social welfare programs and has been reduced in a large number of various budget items, are undermining the State's management capacity in various areas in an alarming way. Specifically, the reduction in the provision of health services is cause for concern. Moreover, the Government's capacity to invest in infrastructure has been significantly reduced; this could be detrimental to the growth potential of the economy taking into account the poor condition of hospitals, airports, roads, ports and railways in the country. It must also be taken into consideration that the state-owned oil company, Pemex, requires significant investment to reverse its financial decline and the downturn in hydrocarbon production. The solution to Pemex's problem calls for resuming private investment for most of the company's projects.

In the coming years, the challenge will be considerable: to maintain public finances in order, reverse the aforementioned decline of the public management capacity, and invest more, particularly in education and healthcare, in a context where fiscal pressure will be on the rise due to increased spending on pensions and debt servicing.

In light of the foregoing, I believe that high-level tax reforms should be implemented. A State that only manages to collect 14% of the GDP cannot aspire to carry out the public investment required to achieve higher growth rates. The main challenge lies in reducing informality and tax evasion: more than half of the economically active population, and 90% of businesses, are informal. It is imperative that this challenge be met.

DISCLAIMER

This document has been prepared by BBVA Research Department. It is provided for information purposes only and expresses data, opinions or estimations regarding the date of issue of the report, prepared by BBVA or obtained from or based on sources we consider to be reliable, and have not been independently verified by BBVA. Therefore, BBVA offers no warranty, either express or implicit, regarding its accuracy, integrity or correctness.

Any estimations this document may contain have been undertaken according to generally accepted methodologies and should be considered as forecasts or projections. Results obtained in the past, either positive or negative, are no guarantee of future performance.

This document and its contents are subject to changes without prior notice depending on variables such as the economic context or market fluctuations. BBVA is not responsible for updating these contents or for giving notice of such changes.

BBVA accepts no liability for any loss, direct or indirect, that may result from the use of this document or its contents.

This document and its contents do not constitute an offer, invitation or solicitation to purchase, divest or enter into any interest in financial assets or instruments. Neither shall this document nor its contents form the basis of any contract, commitment or decision of any kind.

With regard to investment in financial assets related to economic variables this document may cover, readers should be aware that under no circumstances should they base their investment decisions on the information contained in this document. Those persons or entities offering investment products to these potential investors are legally required to provide the information needed for them to take an appropriate investment decision.

The content of this document is protected by intellectual property laws. Reproduction, transformation, distribution, public communication, making available, extraction, reuse, forwarding or use of any nature by any means or process is prohibited, except in cases where it is legally permitted or expressly authorised by BBVA.

ENQUIRIES TO:
BBVA Research: Calle Azul, 4 Edificio La Vela, Floors 4 & 5 28050 Madrid, Spain
Tel. +34 91 374 60 00 y +34 91 537 70 00 / Fax (+34) 91 374 30 25
bbvaresearch@bbva.com www.bbvaresearch.com