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PROSPECTS 2016: Mexico and Central America

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Abstract

Prospects for Mexico and Central America in 2016.

Mexico and Central America will weather the economic slowdown that is affecting many emerging economies in 2016, with most countries doing well by broader regional standards. Security and governance are causes for concern regionwide. Both criminal and state violence will be major issues in Mexico and northern Central America, with increasing migration giving organised crime groups opportunities to diversify and potentially spread south, and heavy-handed policing exacerbating insecurity. Border security issues have the potential to strain relations between countries, while allegations of corruption will challenge governments, with numerous politicians potentially facing trial.

Full text

SUBJECT:Prospects for Mexico and Central America in 2016.

SIGNIFICANCE:Mexico and Central America will weather the economic slowdown that is affecting many emerging economies in 2016, with most countries doing well by broader regional standards. Security and governance are causes for concern regionwide. Both criminal and state violence will be major issues in Mexico and northern Central America, with increasing migration giving organised crime groups opportunities to diversify and potentially spread south, and heavy-handed policing exacerbating insecurity. Border security issues have the potential to strain relations between countries, while allegations of corruption will challenge governments, with numerous politicians potentially facing trial.

ANALYSIS: Strategic summary.

Any unexpected slowdown of the US economy would hit Mexico particularly hard, given the strong integration of manufacturing with US industry.

With unemployment figures falling in the United States, remittances (crucial for several Central American countries) are unlikely to diminish.

Corruption could become a rallying flag for populations region-wide, although further regime changes are highly unlikely.

Many countries' public debt may require tighter fiscal consolidation in 2016, particularly if global liquidity is reduced.

Violent crime will be compounded by tough security policies which, though popular with the public, are ineffective and raise the risk of human rights abuses.

While steady economic growth may placate populations to some extent in the coming year, issues of security and corruption will present major challenges for the region's political parties.

Politics and corruption.

Thirteen Mexican states will elect new governors in 2016, forcing President Enrique Peña Nieto's centre-right Institutional Revolutionary Party (PRI) to defend numerous political posts.

Mexico.

The centre-right National Action Party (PAN) and the centre-left Party of the Democratic Revolution (PRD) changed their leaders recently, and will undoubtedly aim to stage a comeback from their current lacklustre status (see MEXICO: New leaders will bring no real change - October 1, 2015).

That will be particularly challenging for the PRD, with the relatively new Movement for National Regeneration (MORENA) splitting the leftist vote. However, the PAN too is plagued by internal dissent and disagreement, which will seriously hinder its chances of capitalising on public discontent with the PRI.

Moreover, despite widespread outrage over corruption and human rights abuses, recent opinion polls have looked relatively favourably on Peña Nieto.

With opposition parties weak and equally tainted, the PRI will probably poll relatively well in local elections.

Central America.

In Guatemala, President-elect Jimmy Morales -- who takes office in mid-January -- will face a tough task given his political inexperience and the anti-corruption wave that catapulted him to power.

Though he will likely defer much of the transparency fight to the UN's International Commission Against Impunity in Guatemala, the public will demand progress quickly and the slightest hint of improper conduct on Morales's part will be amplified by accusations of hypocrisy.

Meanwhile, unrest will increase in Nicaragua as November's 2016 presidential election draws nearer (see NICARAGUA: Crime falls but political unrest will rise - October 12, 2015), and in Honduras, anti-corruption protesters -- inspired by the ousting of former Guatemalan President Otto Perez Molina -- will increase pressure on their own President Juan Orlando Hernandez (see HONDURAS: Hernandez faces multiple pressures - August 26, 2015).

While incarcerations of former political figures across the region will act as a warning to those who remain, a failure to tackle the structures that enable widespread corruption to take place will see it continue.

Heightened sensitivity on the issue is likely to trigger destabilising, debilitating, and often false accusations with those in high-level positions most at risk of being targeted.

Sober macroeconomic panorama.

The oil price plunge will impact the Mexican economy negatively throughout 2016. By contrast, the fall in oil prices implies a positive terms of trade shock for Central America.

Mexico.

Although Mexico's annual programme of oil hedges will ensure that the government receives at least an average price of 49 dollars/barrel during the year, state oil company Pemex's finances will fall even further into the red.

Moreover, the attractiveness of the sector for domestic and foreign investors has diminished and will be lacking for as long as oil prices remain low.

Even at the guaranteed floor of 49 dollars/barrel, the exchequer's heavy dependence on oil-related revenues will see public finances suffer. The fiscal deficit is expected to fall to 3.0% of GDP during 2016 (from 3.5% this year).

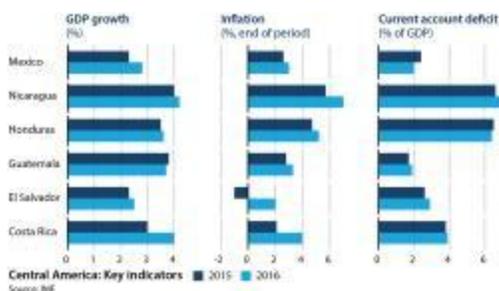
While total public revenues are expected to be roughly constant in real terms, a near-2% contraction in spending is planned. The tightening of fiscal policy should take some steam out of economic growth (see MEXICO: Fiscal package for 2016 is realistic - September 18, 2015).

A positive macroeconomic element is low inflation, which during 2016 should hover around the Bank of Mexico's 3.0% target (it currently stands at 2.5%).

With wage settlements traditionally in the 4-5% range, a small but positive boost to real wages is taking place.

Central America.

Both Costa Rica and Nicaragua are expected to grow around 4% in 2016, with inflation being only slightly high in Nicaragua, where it will edge up marginally to about 7% (see COSTA RICA: Political gridlock undermines reform - August 21, 2015).



Dollarised El Salvador will be the worst regional performer in terms of growth, and could see exports suffer as the dollar strengthens. Nevertheless, growth should still register around 2.5%, slightly above the 2.3% expected for this year.

Security challenges.

Increased migration through the region has the potential to create significant border security issues in 2016, straining relations between neighbouring countries.

With joint US-Mexico migration strategies tightening Mexican borders, Mexico is at risk of becoming a buffer zone that bears the brunt of the migrant influx (see MEXICO/CENTRAL AMERICA: Policies will fail migrants - November 17, 2015). That could greatly exacerbate existing human rights abuses and security problems.

Public safety is an area in which the Pena Nieto administration is clearly failing. With 140,000 killings in the last eight years, the government's militarised response to cartel violence has so far only made matters worse.

'Iron fist' policies have exacerbated violence wherever they have been employed, with the breakdown of El Salvador's 2012 gang truce and the consequent shift towards a hardline stance by the Salvadoran government seeing murder rates skyrocket in that country in particular (see EL SALVADOR: Soaring violence prompts security rethink - May 11, 2015).

The UN has called for a demilitarisation of policing in Mexico, with the Mexican military's dismal human rights record drawing international scrutiny and spurring investigations into extrajudicial killings.

However, accusations of corruption and incompetence in local police forces will increase the temptation to rely on the military, which, despite facing its own scandals, is at least centrally controlled.

Clashes between drug cartels and security forces will therefore represent a continued struggle for the government and population alike, with high death tolls set to continue and Mexico's human rights record unlikely to see any significant improvement in 2016.

CONCLUSION: Mexican GDP growth in 2016 is expected to be around 2.8%. However, if the US economy continues to strengthen it should greatly favour both Mexico and Central America, through trade and remittances. The oil-price plunge will have a positive impact on much of the region, excluding Mexico. As a whole, Central America is expected to grow by about 4% in 2016. Politically, public anger over corruption is unlikely to dissipate and will trigger protests across much of the region, which if mishandled could become violent.

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Details

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