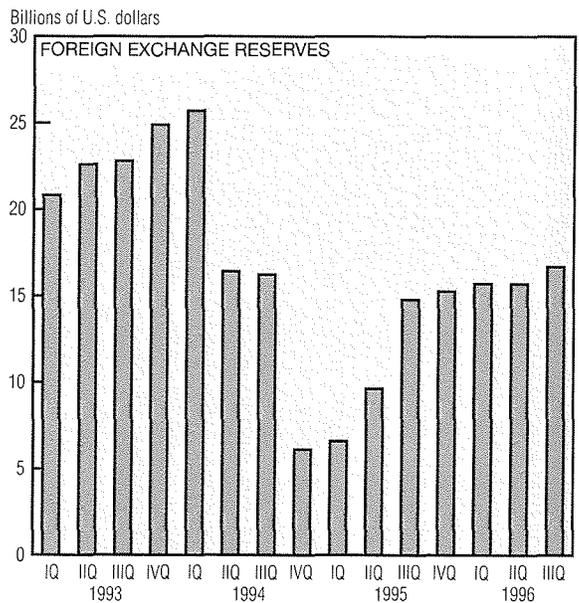
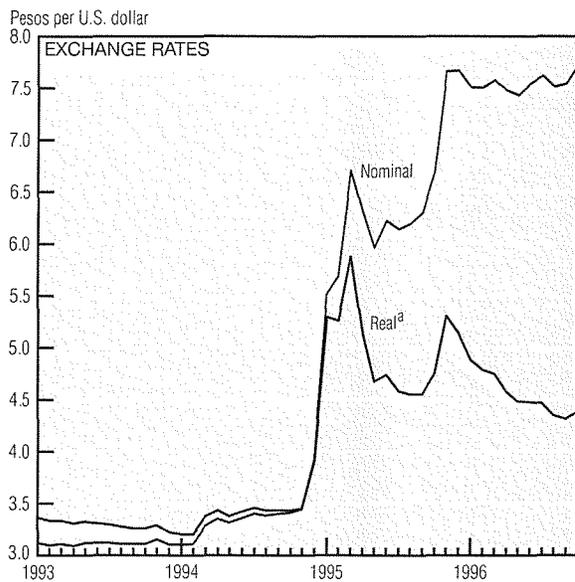
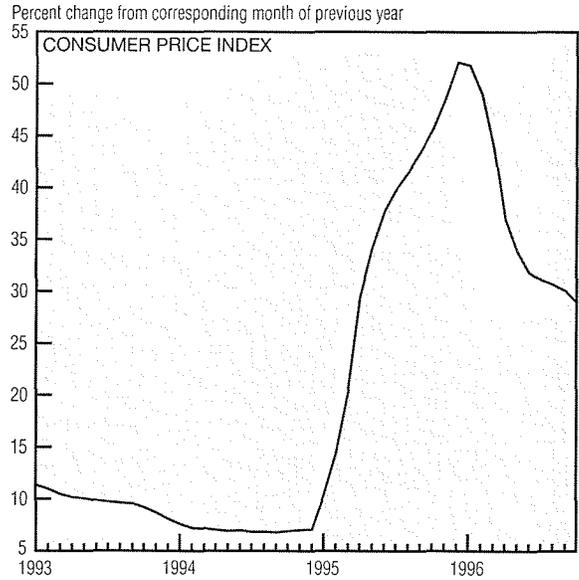
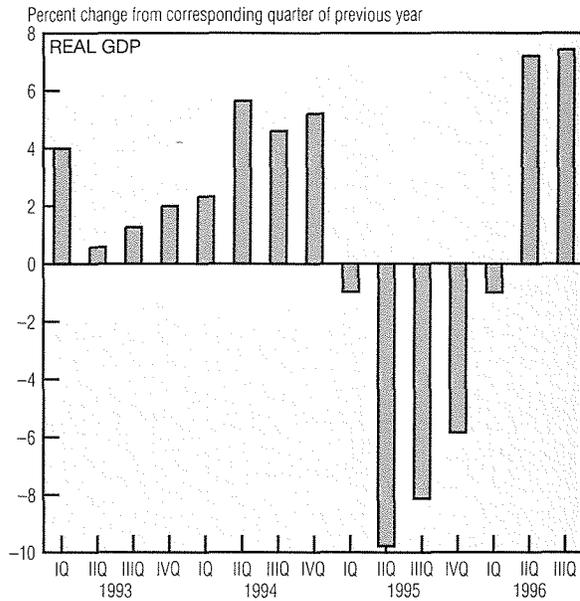


# The Mexican Economy



a. The real exchange rate is calculated using consumer prices for both the U.S. and Mexico. The base period is November 1994.  
 SOURCES: Banco de Mexico; and International Monetary Fund, *International Financial Statistics*.

Two years after the disruptive peso depreciation, the outlook for Mexico is brightening. Our NAFTA partner has regained access to international capital markets and can now repay its creditors. Of continuing concern, however, are uncertainties associated with real currency appreciation and with the fragility of the banking sector.

After declining sharply in 1995, real economic activity has rebounded. Much of the growth has

been in the export and investment sectors; consumer spending remains weak. Inflation moderated from an annual rate of 52% in late 1995 to approximately 28% last November.

Mexico's relatively high inflation rate vis-à-vis the U.S. has eroded much, but not all, of the price advantage that the peso depreciation conferred on Mexican goods. That the nominal exchange rate remains fairly stable despite continuing price

differentials attests to growing confidence in Mexican monetary policy, which has remained contractionary. Foreign capital inflows are returning, and Mexico's international foreign currency reserves, when valued at current exchange rates, exceed its monetary base. The quality of bank assets, however, remains poor despite efforts at financial reorganization and attempts to boost liquidity and improve capital.