



The construction sector accounted for around 6.1m direct jobs in 2018

Foundation for the future

Building activity takes a pause as the government defines its ambitious policy agenda

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With infrastructure development identified as a driver for medium-term growth, construction is tipped to play a major role in the Mexican economy. The country's potential in this area is highlighted in its ranking of 49 out of 140 countries in terms of infrastructure in the "Global Competitiveness Report 2018" published by the World Economic Forum (WEF). Despite this, between 2017 and early 2019 the sector faltered due to a slowdown in civil engineering projects and uncertainty about Mexico's trade relationship with the US.

DRIVERS OF EXPANSION: Construction activity has long been viewed as a bellwether for Mexico's overall economic trajectory. Over the last decade an upwards swing in industrial investment has corresponded with an uptick in construction and a transformation of the landscape in many urban centres. "Mexico City, Monterrey, Puebla, Guadalajara and Querétaro are the cities that are most advanced in terms of urban planning and infrastructure development," José Antonio Hernández Balbuena, director of the Centre for Economic Studies (Centro de Estudios Económicos del Sector de la Construcción, CEESCO) of the Mexican Chamber of Construction (Cámara Mexicana de la Industria de la Construcción, CMIC), told OBG.

The strengthening of transport infrastructure has also resulted in a flurry of construction. Between 2012 and 2018 the Ministry of Communications and Transportation (Secretaría de Comunicaciones y Transportes, SCT) completed 38 new motorways covering 3400 km and 33,000 km of rural roadways. Projects included the widening of the Mexico-Puebla highway, the construction of the new Marquesa-Toluca freeway, and an elevated highway connecting Mexico City to the freeway that leads to Cuernavaca and Acapulco to the west.

SECTOR PERFORMANCE: Construction contributed 8.1% to GDP in the first quarter of 2019, according to the National Institute of Statistics and Geography, and in 2018 the sector expanded by 0.6%, trailing the country's overall GDP growth of 2%, according to figures

provided by the CMIC. Meanwhile, in June 2019 BBVA México forecast the construction sector to expand by 2% in 2019 as energy and transport projects proposed by the federal government are completed. This growth is a shift from 2017, when construction contracted by 0.8%, the first time the sector shrunk had since 2013. "There are significant numbers of developers who are putting the brakes on activity," Jesús Orozco, CEO at Tinsa México, a Mexico City-based real estate investment advisory firm, told OBG. Some of the pause is a result of real estate developers and investors waiting for the administration of President Andrés Manuel López Obrador – commonly known as AMLO – to signal an overall infrastructure strategy that would lay out a clearer path to development.

Public works decreased by 5.8% in 2018, while private sector construction activity increased by 1.3% the same year. Between December 2018 and April 2019, construction activity declined by an average of 2.1%, dropping by 1% in February, by 2.5% in March and by 4.2% in April. However, housing construction grew by 3.2% in the first quarter of 2019. There has been sustained construction in housing since 2014, which has fuelled an increase in demand. The rise in housing demand was also reflected in a 1.1% increase in mortgage financing in 2018, according to BBVA México.

In 2018 and early 2019 construction continued to be a major contributor to economic growth, even as overall levels of activity and investment faltered. "The construction sector is one of Mexico's most important economic drivers, being the fourth largest contributor to the country's GDP, and with a multiplying effect on three out of four productive industries in the economy," Eduardo Ramírez Leal, president of CMIC told OBG.

In the first quarter of 2019 public works expenditure in Mexico reached MXN64bn (\$3.3bn), with Campeche, Oaxaca and Chiapas benefitting the most from public infrastructure investment during this period. While public spending fell by 13.1% in the first quarter

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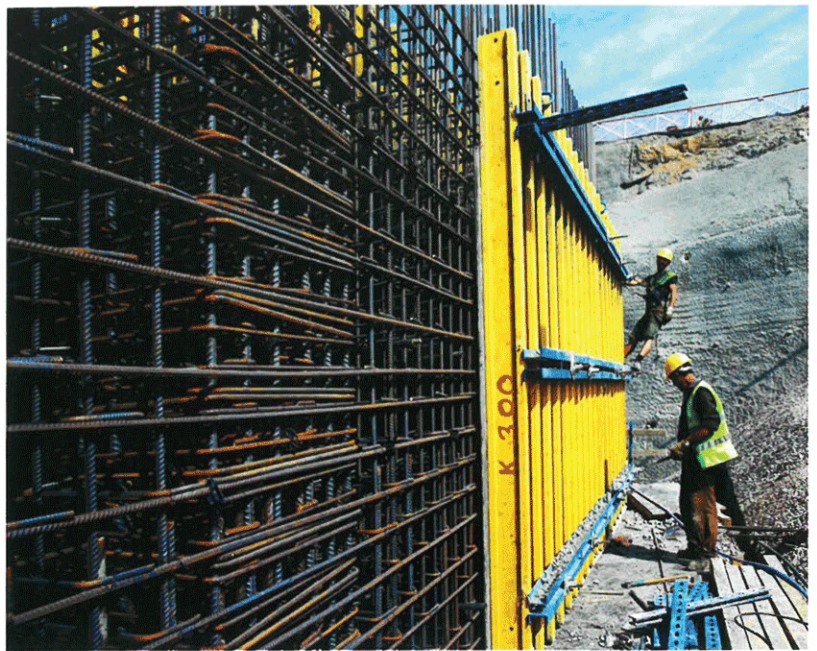
of 2019, overall levels of private sector construction spending increased by 8.3%. Notably, during this period the private sector made up 62% of total construction investment, with Quintana Roo, Querétaro and Jalisco receiving the largest shares of private investment as a percentage of total infrastructure spending. The dominance of private investment is expected to continue, with the government estimating it could account for 83% of expenditure by 2024.

The sector accounted for around 6.1m direct jobs and 3.1m indirect jobs in 2018. This figure is expected to increase to 6.5m direct jobs and 3.3m indirect jobs by 2022, according to figures from the CMIC. Importantly, construction was the third-most-important job creator in Mexico, after agriculture and commerce.

However, even though the sector is an important contributor to the economy, construction standards still lag behind more developed economies. "Construction standards in Mexico are a long way behind other large economies," Raúl Berarducci, CEO of Bovis, a project management and construction company, told OBG. "The root of the problem is the lack of authority needed to oversee and enforce regulations. The sector needs better institutional capacity with more people overseeing procedures to ensure all safety standards are met."

MAJOR PROJECTS: Throughout the first nine months of 2019 AMLO announced a trio of flagship projects to drive growth. He proposed building an airport in Santa Lucía, around 50 km north of the existing Mexico City International Airport (Aeropuerto Internacional de la Ciudad de México, AICM), which is over capacity. At a cost of MXN78.6bn (\$444.7m), the proposed Santa Lucía airport was expected to have a maximum annual passenger capacity of 20m to offset AICM's passenger load; however, in August 2019 a judge issued a ruling that suspended construction. Later the same month a judge overruled the environmental approval given to the Santa Lucía airport by the Ministry of Environment and Natural Resources in July 2019. The path forward is unclear after a series of legal challenges and setbacks, but in September 2019 AMLO told local media that he expects soon there will be "no legal obstacle" to its construction. The president also announced plans for the Maya Train project, which would transport both tourists and cargo around the Yucatán Peninsula, and a new \$8bn refinery for the state-owned oil company Petróleos Mexicanos in Tabasco along the northern coast, with a capacity to process over 300,000 barrels of crude oil a day. The new refinery is also part of the president's drive to increase domestic fuel production and decrease reliance on imports.

AIRPORT DISPUTE: In a referendum held in October 2018 voters rejected the completion of the partially built multibillion-dollar New Mexico City International Airport 25 km north-east of Mexico City, which caused work to come to a halt. Furthermore, AMLO had argued that the project was tainted by corruption and geologically unsound. The \$13bn airport was expected to have a capacity for 100m passengers a year and be completed in 2020 and was touted as a catalyst for other sizeable urban development projects such



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as shopping malls, hotels, residences, hospitals and connecting transport infrastructure.

RAIL: Mexico presents significant opportunities for investment in rail infrastructure, with 26,891 km of track as of 2017. Nearly three-quarters of this rail system was built in 1910, with 278 km of track built between 1995 and 2018. However, only 23,366 km of track is operational. Rail is also lightly utilised. "Mexico needs a long-term plan for its railway network," Luis Rojas Nieto, CEO of civil engineering firm Freyssinet de México, told OBG. "The current concession model is working well, but it needs to be incorporated into a new model, one with more concrete, long-term outcomes. Over 85% of cargo is still transported by road, and this needs to be reduced," he continued.

There are opportunities for new investments to connect ports to existing rail networks, as well as expand and build new rail lines. The government has signalled its openness to working with private investors to build new infrastructure. One of AMLO's main projects is the Trans-Isthmus railway, which will connect the deep-water ports of Coatzacoalcos in the Gulf of Mexico with the Salina Cruz port on the Pacific. The SCT was awarded a budget of MXN645m (\$33.4m) to begin the railway's development. The project, which is set for completion in 2021 and expected to cost \$11bn, will pass through underdeveloped areas of southern Mexico, and will include six new development and innovation zones along the new rail line. The railway is to be accompanied by a raft of infrastructure projects aimed at creating a trade corridor, including a natural gas pipeline, and road and port upgrades.

Mexico's other flagship railway project is the Maya Train. The project, already under way, will construct seven train lines running a total of 1470 km through the states of Quintana Roo, Tabasco, Campeche, Chiapas and Yucatán at a cost of MXN150bn (\$7.8bn). "The Maya Train could be a catalyst for tourism," Orozco told OBG. The government has also pledged support for the

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completion of the Line 3 light rail system in Guadalajara, allocating MXN4.5bn (\$232.7m) to ensure the project is operational by the end of 2019. The system will span 21.5 km and connect 18 stations in the municipalities of Tlaquepaque, Zapopan and Guadalajara. The lines will include 18 trains, each holding up to 2100 passengers and serving a total of 233,000 riders a day. "We are adamant about finishing projects as soon as possible," AMLO said at a press conference for the project in February 2019. "We made the decision to put resources together and make finishing this project a priority." Other endeavours include the \$3.2bn Mexico City-Toluca commuter rail project, and an above-ground rail link that will connect the Observatorio metro station in the capital to the Mexico City-Toluca train line.

MOTORWAYS: Mexico has an extensive network of federal and state trunk roads. The country relies heavily on highway infrastructure for moving passengers and cargo. In 2018 the country's stock of highways included 50,435 km of federal highways, 101,460 km of state

highways, 10,557 km of toll highways and 19,452 km of other types of highways. The government has promised to invest in road infrastructure improvement projects, and notably complete a transnational highway link to Mexico's Pacific and Atlantic coasts. The project will require a MXN120m (\$6.2m) expansion of the Salina Cruz-Coatzacoalcos highway. Indeed, over the medium term Mexico is likely to see additional investment in new highways, with funding coming from both the public and private sectors. "Highway infrastructure is one of the clearest examples of Mexico's development," Hernández Balbuena of CEESCO told OBG. "Within Latin America, Mexico is one of the countries that has made the most progress in highway development, although there remains room for improvement."

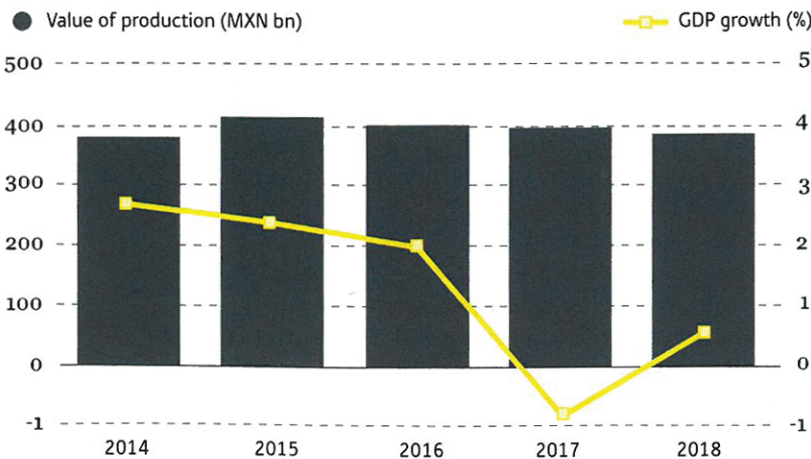
In December 2018 the government released its National Highway Infrastructure Programme, with plans to build 5531 km of new highways at an investment of MXN14.2bn (\$734.3m) by 2024 (see Transport & Logistics chapter). "The first priority will be maintaining infrastructure and the second will be finishing incomplete projects," AMLO explained at a press conference announcing the initiative that month. The plan includes efforts to build roadways to connect 300 rural communities in Mexico's five least-developed states. Indeed, rural areas hold significant opportunities for building new roads and highways to connect isolated farming communities to the existing expressway networks. "One thing we need is investment in infrastructure, as it is still difficult to move harvests from the centre of the country," Alberto Cuéllar, director of economic studies at the Ministry of Agriculture and Rural Development, told OBG. "We need more roads, highways and state highways – rural highways are below optimal."

PORTS: Over the last decade federal and state governments have invested significant resources in building and expanding major ports. Between 2012 and 2018 Mexico rose from 75th to 57th out of 140 countries in the WEF's Global Competitiveness Index in terms of port infrastructure. The SCT estimates that 80% of the funding for port expansion projects in the same period came from the private sector. Looking to the coming years, the government plans to develop eight new seaports before 2025.

OUTLOOK: To confront the risk and uncertainty stemming from a variety of external and internal factors, Mexico should develop a clearly defined strategy for developing infrastructure and promoting sustainable, long-term growth. To do so, according to a March 2019 CEESCO report, the country should boost public investment at the local, state and federal levels, as well as accelerate the pace of public bidding.

With federal authorities breaking ground on flagship projects, state and local governments are promoting infrastructure investment as part of their long-term industrial development strategies. Although uncertainty clouds the outlook for the national economy, opportunities exist at the local level. State and local governments have helped boost infrastructure investment and industrial development, and the dynamism of these industrial hubs is likely to continue to spur demand.

Construction activity, 2014-18



Source: INEGI & CMIC