

Modest growth due to subdued industrial activity in the US and low oil

General Information



GDP	USD1144.3313bn (World ranking 15, World Bank 2015)
Population	127.02mn (World ranking 10, World Bank 2015)
Form of state	Federal Republic
Head of government	Enrique PENA NIETO (PRI)
Next elections	2018, presidential



Strengths

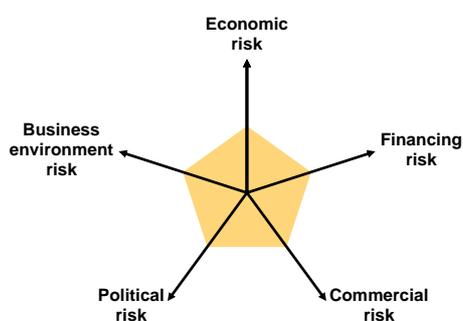
- Sound macro-policy framework
- Moderate debt ratios
- Strong, pro-business reform dynamics
- Structural business environment exceeds Latin American average
- Durable political framework with stable handovers of power
- Member of OECD
- Easy access to capital markets
- Support from IFIs likely if needed

Weaknesses

- Fiscal position highly sensitive to oil price (>30% of public revenues)
- Sensitive to US business cycle (>80% of exports)
- Skewed income distribution (geographically as well as among socio-economic groups), still high poverty levels
- Security issues related to drug-trafficking
- Rule of Law and control of corruption below Latin America's average

Country Rating

BB2



Source: Euler Hermes

Trade Structure

By destination/origin (% of total)

Exports	Rank	Imports
United States	80% 1	49% United States
Canada	3% 2	17% China
China	2% 3	4% Japan
Spain	1% 4	3% Korea, Republic of
Brazil	1% 5	3% Germany

By product (% of total)

Exports	Rank	Imports
Crude Oil	10% 1	7% Electrical Apparatus
Electrical Apparatus	8% 2	6% Refined Petroleum Products
Cars And Cycles	8% 3	6% Telecommunications
Commercial Vehicles	8% 4	6% Vehicles Components
Vehicles Components	6% 5	6% Engines

Sources: ITC, Chelem

Economic Overview

Subdued GDP growth

Real GDP expanded by a moderate +2.5% in 2015, after +2.2% in 2014. The primary and tertiary sectors performed well in 2015 and expanded by +3.0% and 3.3% respectively, while the industrial sector disappointed with +1.1% growth.

Mexico continues to lose momentum rapidly. Real GDP contracted for the first time in three years in Q2 2016, by -0.5% q/q, after expanding by a modest +0.8% in Q1. Private consumption has proved quite resilient. Retail sales expanded rapidly (+8% y/y in July) amid strong consumer confidence. However, the industrial sector continues to underperform and shrunk by -1.5% in Q2, dragged down by laggard US economy (-0.5% y/y in July). Mexico's neighbor to the north absorbs 80% of Mexican industrial exports.

The economy also feels the pinch of tight fiscal and monetary policies. Despite moderate inflation (+2.7% y/y in July), the Central Bank has raised its key policy interest rate by +125bps to 4.25% since December 2015. This was done to smoothen the impact of external shocks on the currency, with the risk of a Fed rate hike in mind. Further hikes in the key rate are expected. At the same time, the government has announced several cuts in the budget due to still low oil revenues and investors' concerns about public finances. Overall, spending cuts worth more than 1pp of GDP have been declared since the start of the year.

All in all, we expect the Mexican economy to grow by +1.7% in 2016 and +2.2% in 2017.

External balances have deteriorated

Ongoing low oil prices and disappointing economic activity in the US are weighing down on exports. The effect is significant: -7% since late-2014. The trade deficit has widened to -USD1.8bn in July 2016. Only a year and a half ago trade was balanced. The current account deficit is expected to widen to -3% in 2016, and to reach -2.8% in 2017.

The Mexican peso is underperforming and will continue to be plagued by high volatility. Along with the Argentine peso, the MXN is the only important LATAM currency to have depreciated against the USD since the beginning of the year. It is particularly vulnerable to external shocks and one of emerging markets' most liquid currencies.

However, external financing should not be a problem. The current account deficit is almost entirely covered by FDI inflows while Mexico benefits from easy access to capital markets and enjoys a Flexible Credit Line by the IMF. Foreign exchange reserves have diminished to USD174bn in July (-7.7% y/y) as the Central Bank has intervened in the FX markets to support the peso. Reserves now cover above 5 months of imports.

The business environment is overall good. Mexico ranks 38th out of 189 in the 2016 World Bank's Doing Business Survey. It is a rather good position when compared with other LatAm peers.

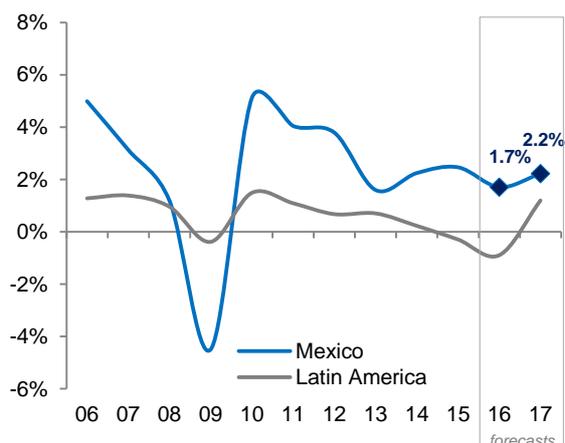
Key economic forecasts

	2014	2015	2016	2017
GDP growth (% change)	2.2	2.5	1.7	2.2
Inflation (% , yearly average)	4.0	2.7	2.8	3.0
Fiscal balance* (% of GDP)	-4.6	-4.1	-3.7	-3.5
Public debt* (% of GDP)	49.5	54.0	57.7	61.2
Current account (% of GDP)	-1.9	-2.8	-3.2	-2.8
External debt (% of GDP)	33.4	39.7	45.2	45.9

*Includes Local Government; Non-financial Public Corporations; Social Security Funds; State Governments

Sources: IHS, Euler Hermes, National Statistics

Real GDP growth (%)



Sources: National sources, IHS, Euler Hermes

Industrial production growth (y/y, %)



Sources: Bloomberg, IHS, Euler Hermes

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