

# Investing in Mexico: Challenges and opportunities

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1. **Macroeconomic outlook**
2. **What are the most salient risks and opportunities in Mexico's leading sectors?**
3. **Infrastructure projects: which could have the biggest impact?**
4. **Mexico as an FDI hub for China**
5. **Final remarks**

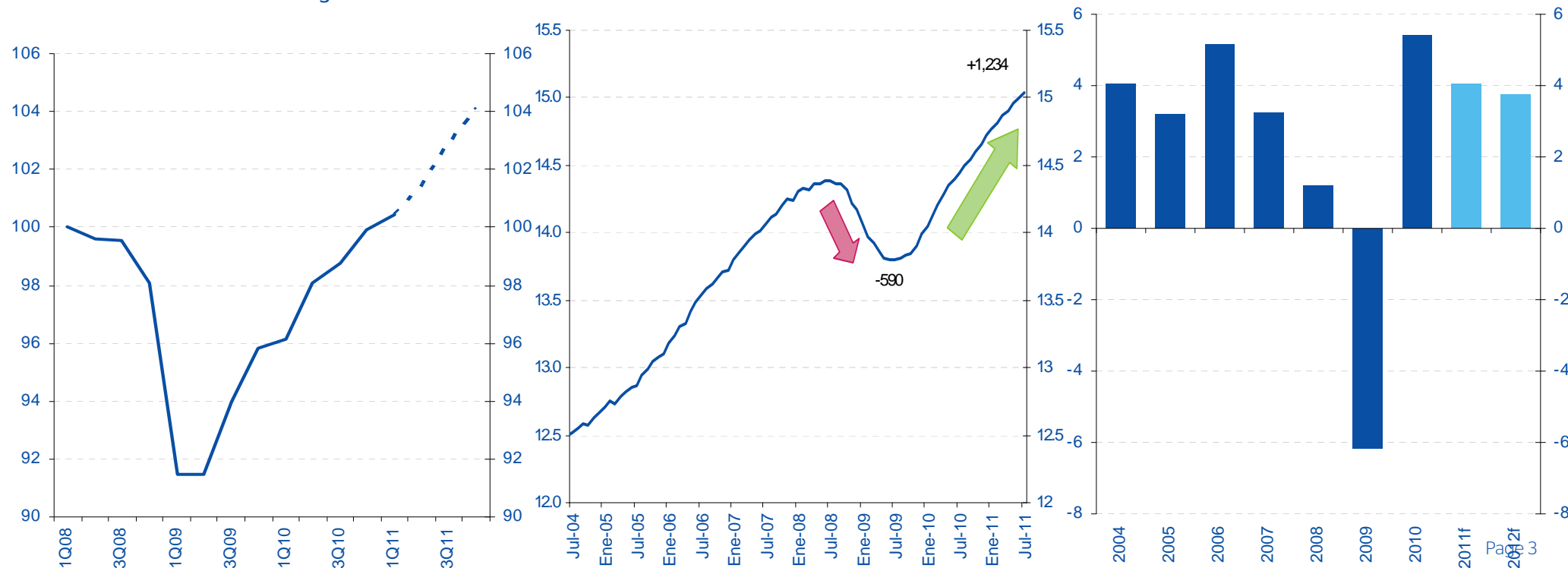
# Higher competitiveness and employment drive the Mexican economy expansion over 4% in 2011-12

- Improved foreign demand, better funding conditions and higher employment to foster domestic demand and economic growth

**Mexico, GDP**  
1Q08=100  
Source: BBVA Research and Inegi

**Employment**  
(Formal market, million people)  
Source: BBVA Research

**Economic Growth**  
Source: BBVA Research and INEGI

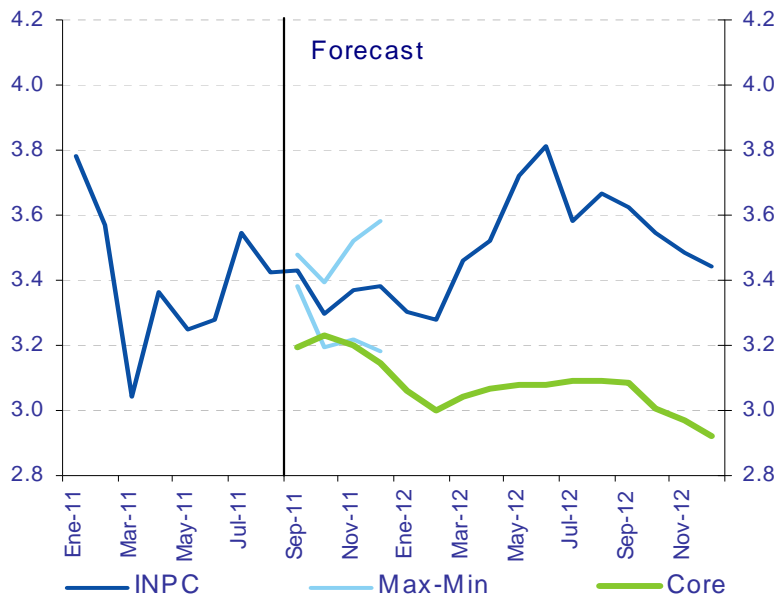


# Financial variables: anchored to stability

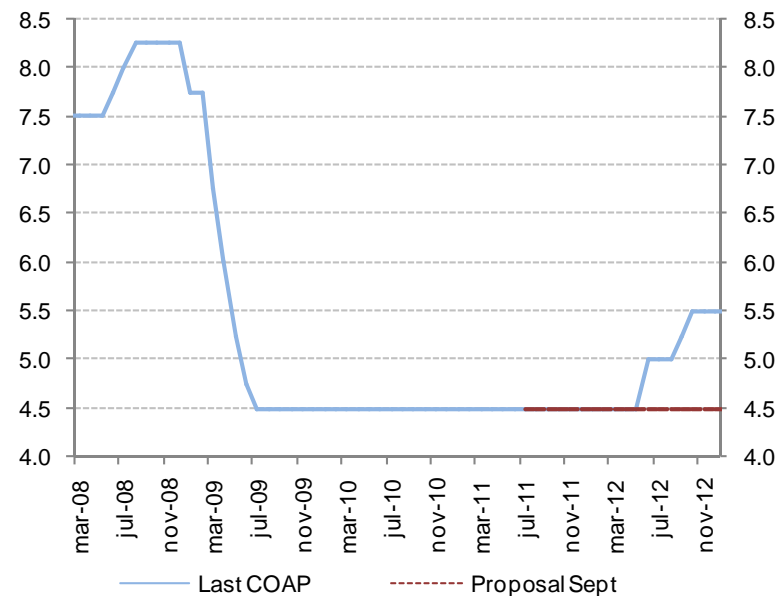
## Anchored mid-term inflation will lead to limited monetary hiking

- Balance of risk of inflation has improved due to: i) Lack of relevant pass-through from demand pressures or commodity prices; ii) Positive surprises on the non-core component
- Banxico's tightening could come not earlier than summer 2012

Mexico. Inflation



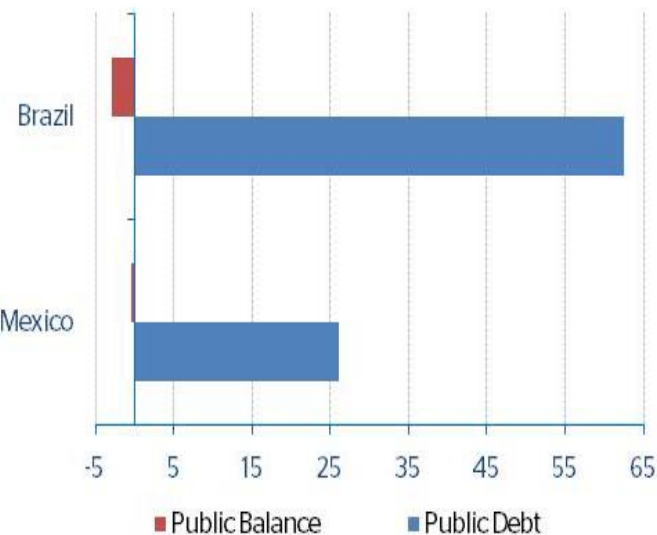
Banxico. Funding rate



# Mexico: reaping the benefits of continued commitment to sound macro policies

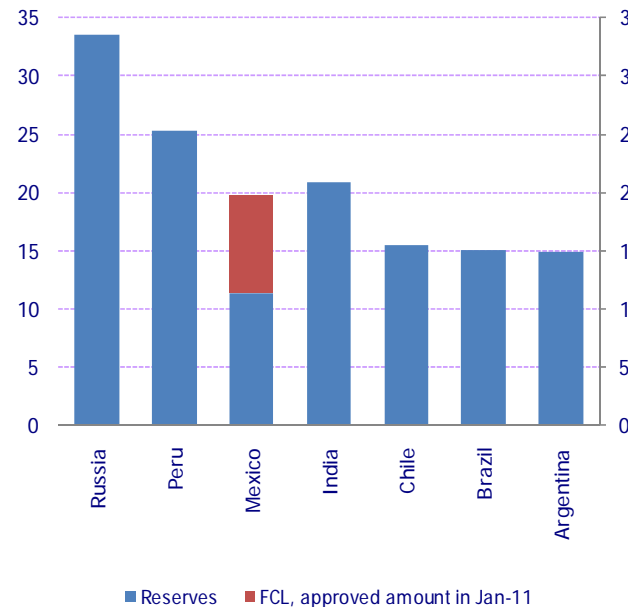
- Non-external imbalances and reliable fiscal policy allow Mexico be supported by IMF through FCL, precautionary USD funding without policy conditionality
- Mexican peso forecasted path is coherent with inflation and growth differentials vs.USA. Mexican authorities engagement to a non-intervention exchange rate policy is a strength regarding other emerging currencies

Public Balance and Debt (% GDP, Average 2005-09)



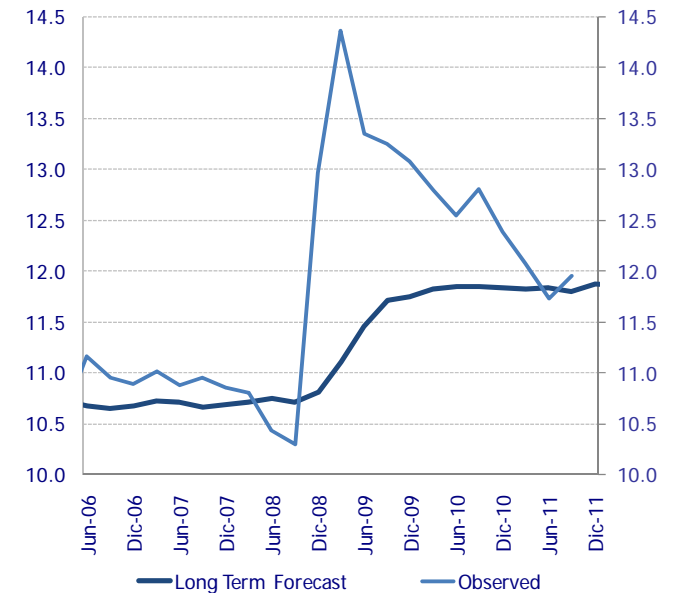
Source: IIF

Availability of USD funding



Source: BBVA Research

Exchange Rate, MXN Peso per USD

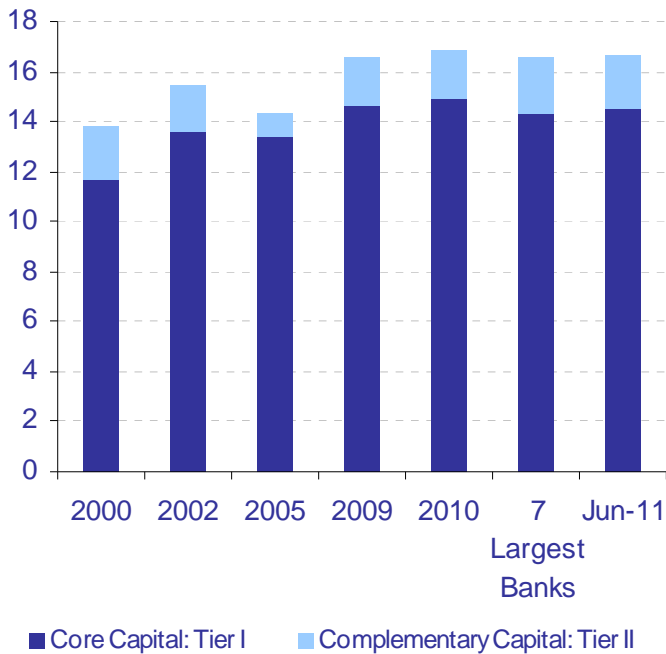


Source: BBVA Research

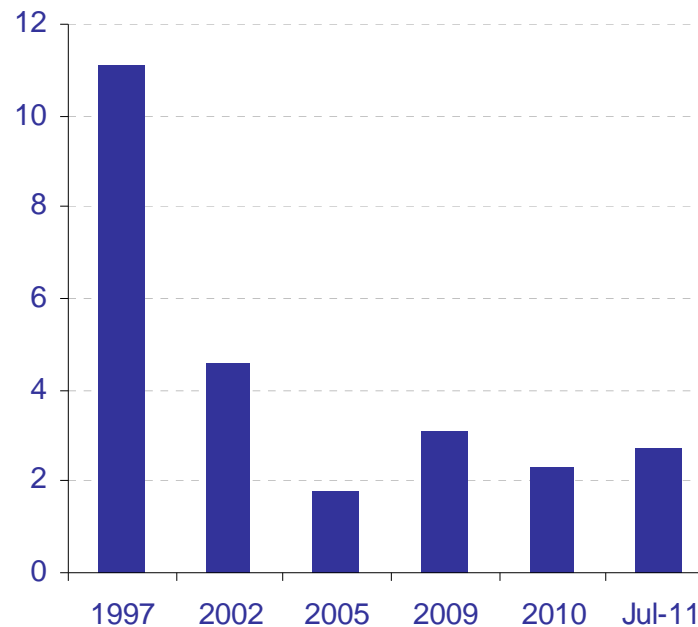
# The Mexican Banking Sector highly capitalized

Credit risk is limited and well covered

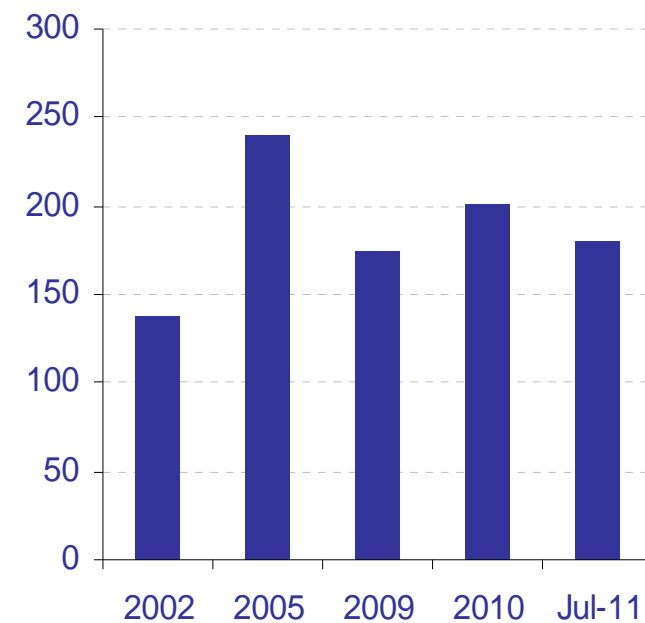
**Capitalization ratio of the Mexican Banking Sector**  
(Percentage of Risk Weighted Assets)



**Bank Nonperforming Loans to Total Loans, %**



**Provisions to Nonperforming Loans, %**

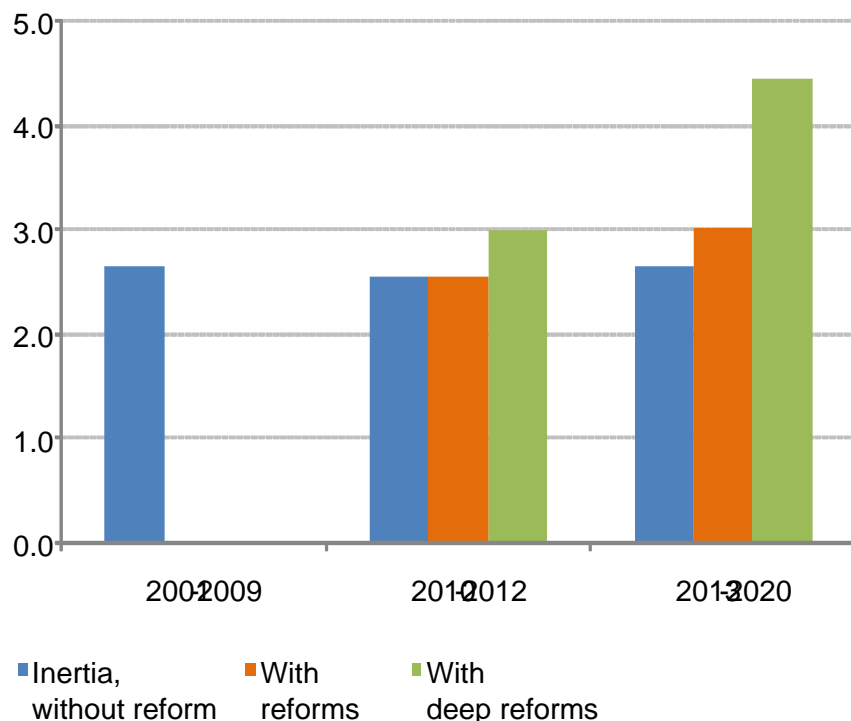


# The challenge is to take advantage of the positive cycle to continue to strengthen the economy

Although the political panorama is not the best to achieve the necessary agreements to bring about reforms, the continued implementation of reforms is the necessary condition to increase Mexico's long-term growth capacity.

Mexico. Alternative growth scenarios according to the intensity of the reform process

Source: BBVA Research



**Fiscal reform to increase income and spending as well as improve their efficiency**

**Political reform to improve responsibility and accelerate legislative procedures**

**Strengthening of the rule of law**

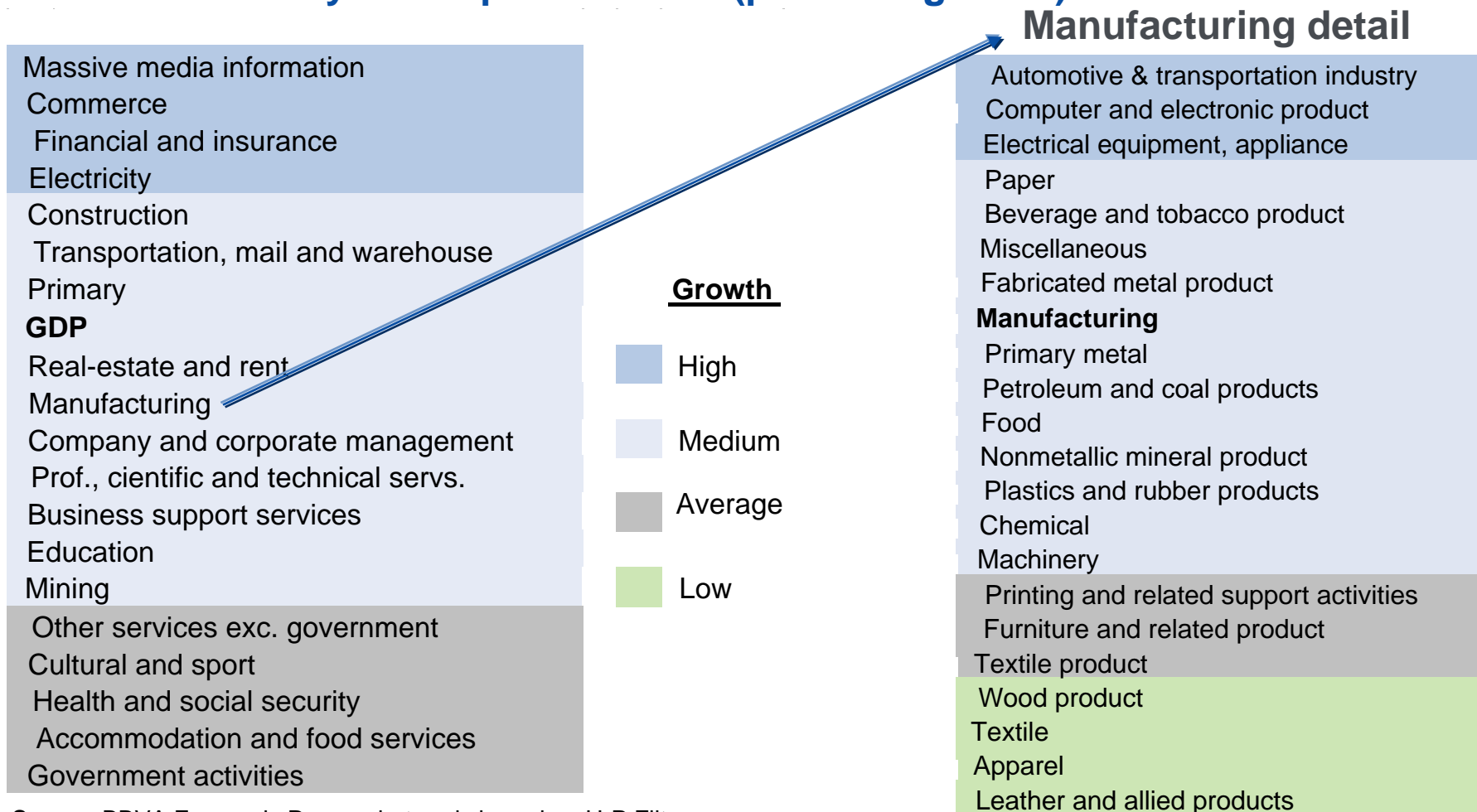
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# Sector Opportunities: commerce, utilities and export oriented manufacturing

From a long-term perspective, export oriented, services and innovative activities could have relatively better performance (potential growth)



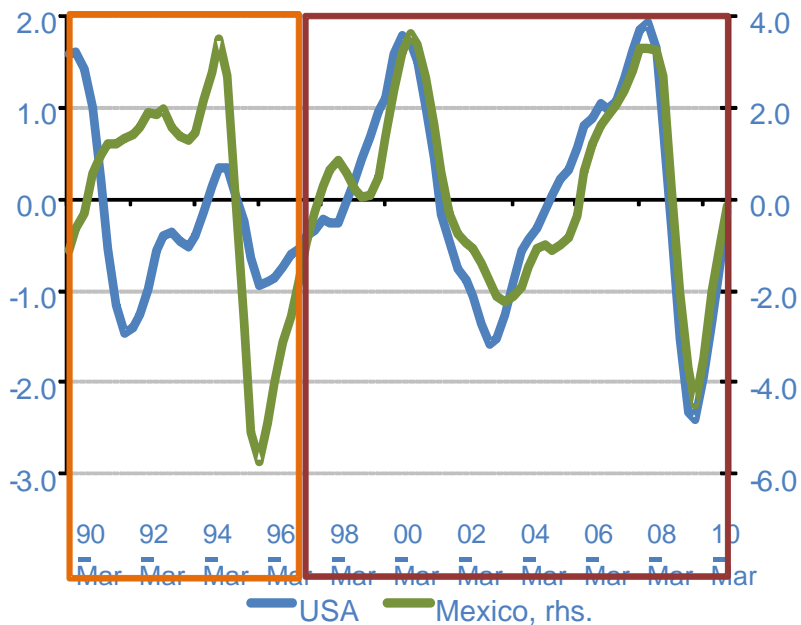
Source: BBVA Economic Research, trends based on H-P Filter

# Key continues to be the US

Mexico and the US maintain a high degree of economic integration, with marketshare advances by Mexico, positioning the country as second supplier of manufactured goods, at the same level as Canada.

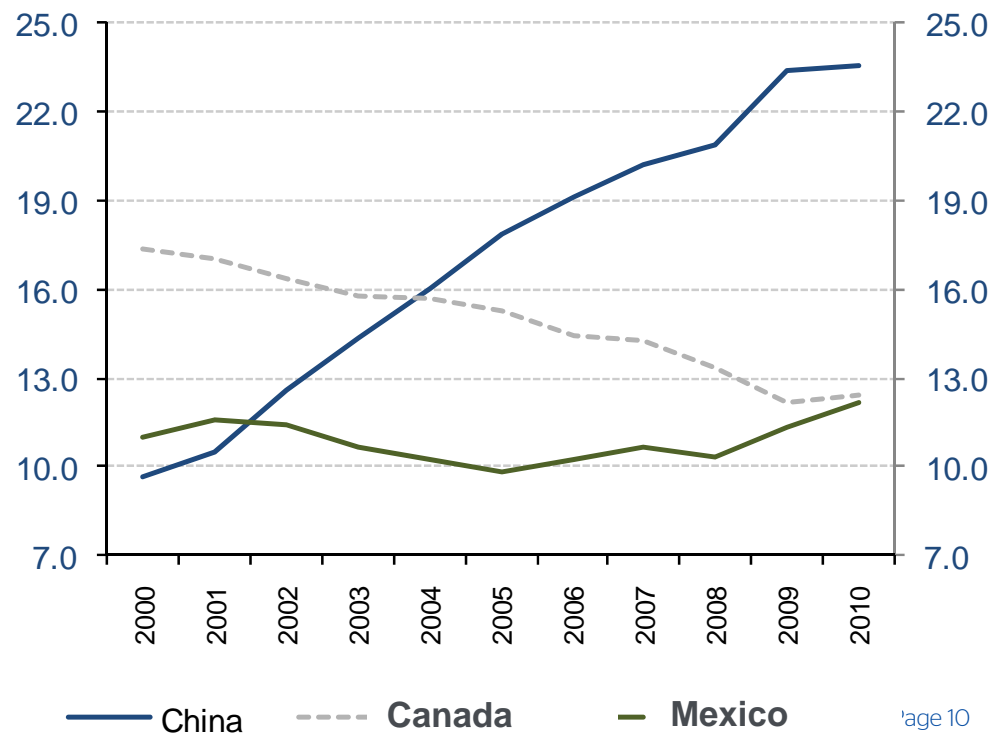
Economic cycle, % Breach with GDP tendency

Source: BBVA Research



Marketshare in US manufacturing market

Source: BBVA Research with INEGI and USTIC data

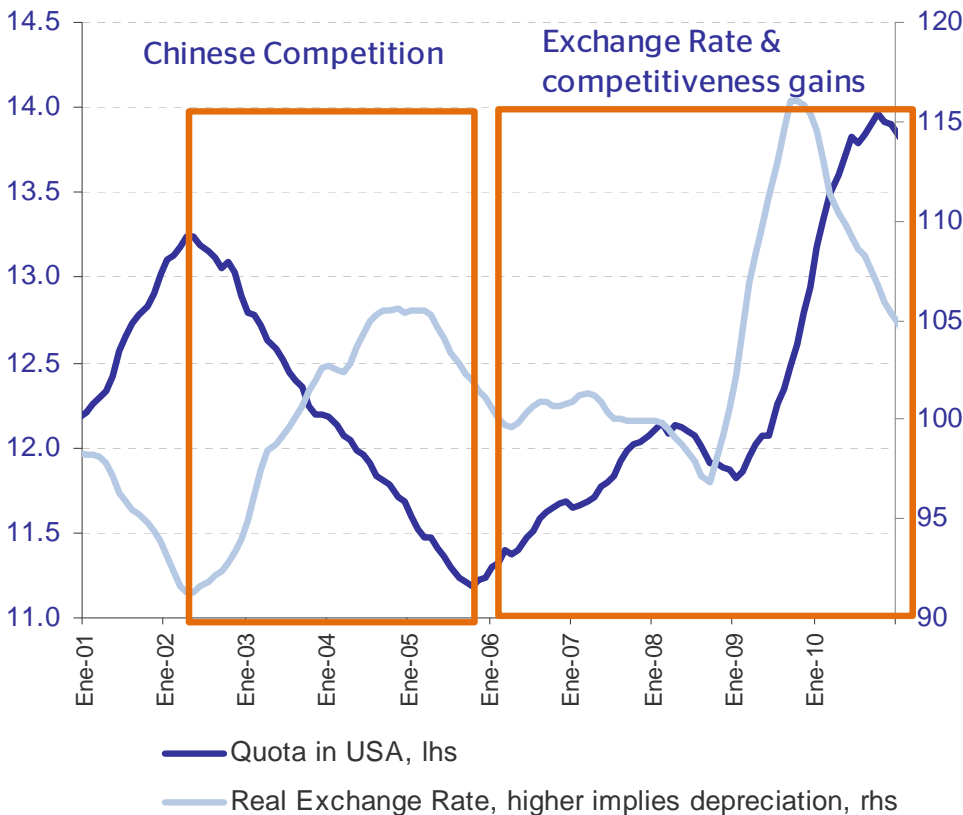


# With improvements in sector competitiveness

The exchange rate is not the sole support to gains in competitiveness. Sectors integrated in transnational value chains that attract FDI further improve their presence in the US manufacturing market.

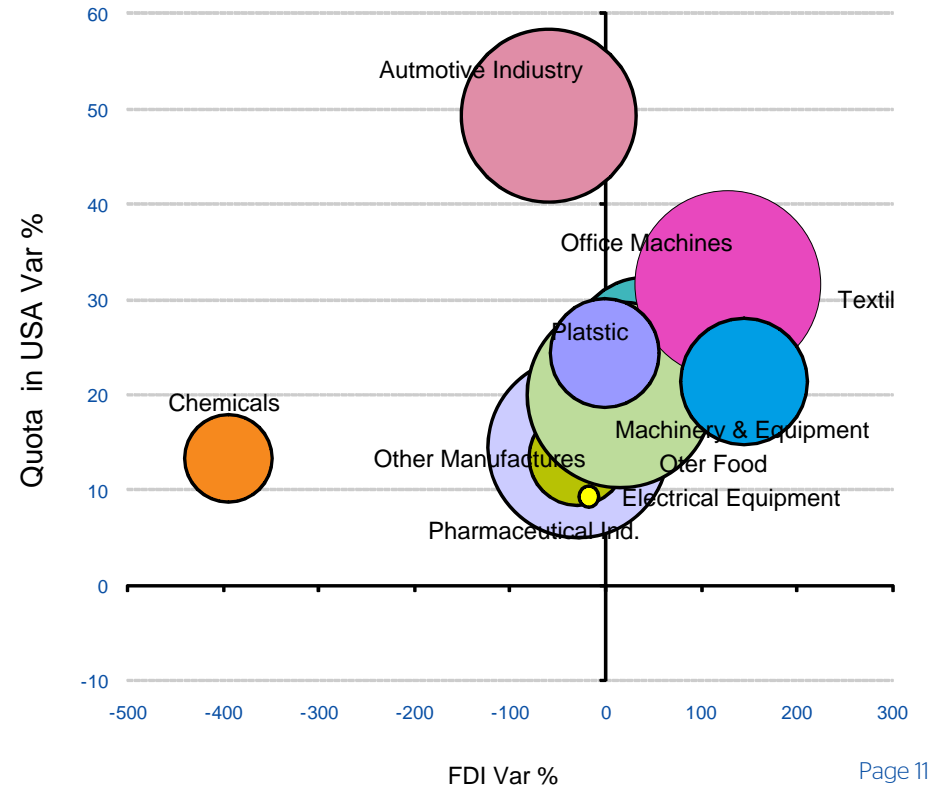
Peso exchange rate and marketshare in US

Source: BBVA Research with Banxico and USITC data



Sectors in Mexico: FDI received and marketshare in US

Source: BBVA Research

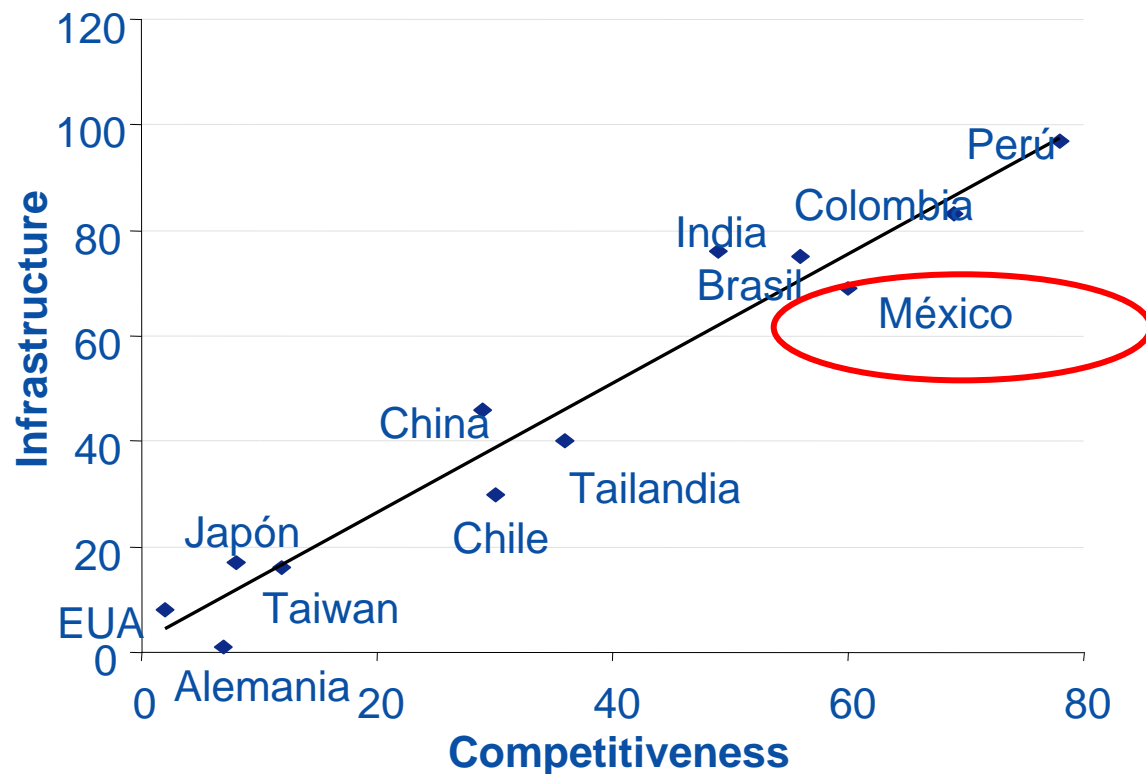


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# Infrastructure, competitiveness and development high correlation

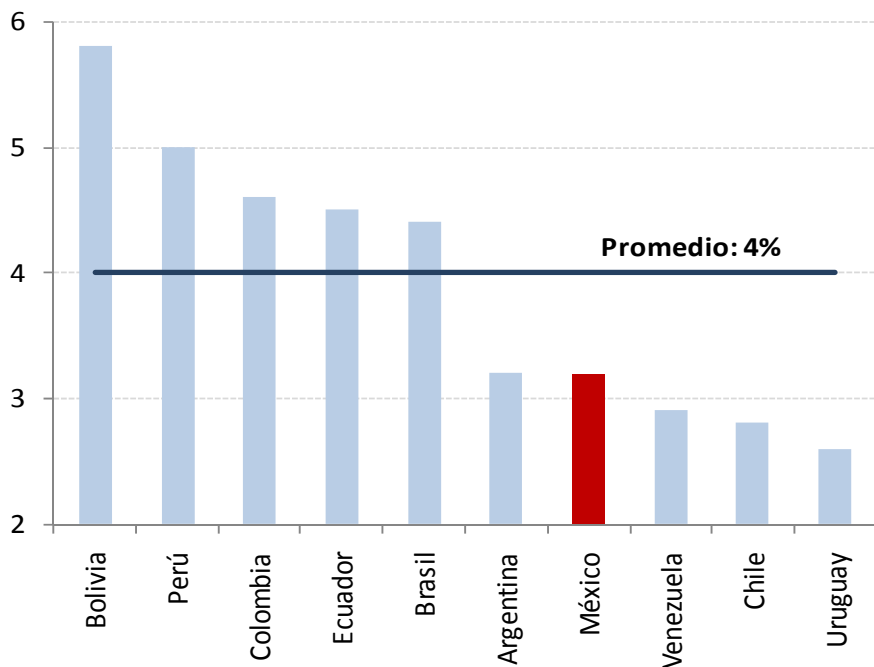
## Infraestructura and competitiveness



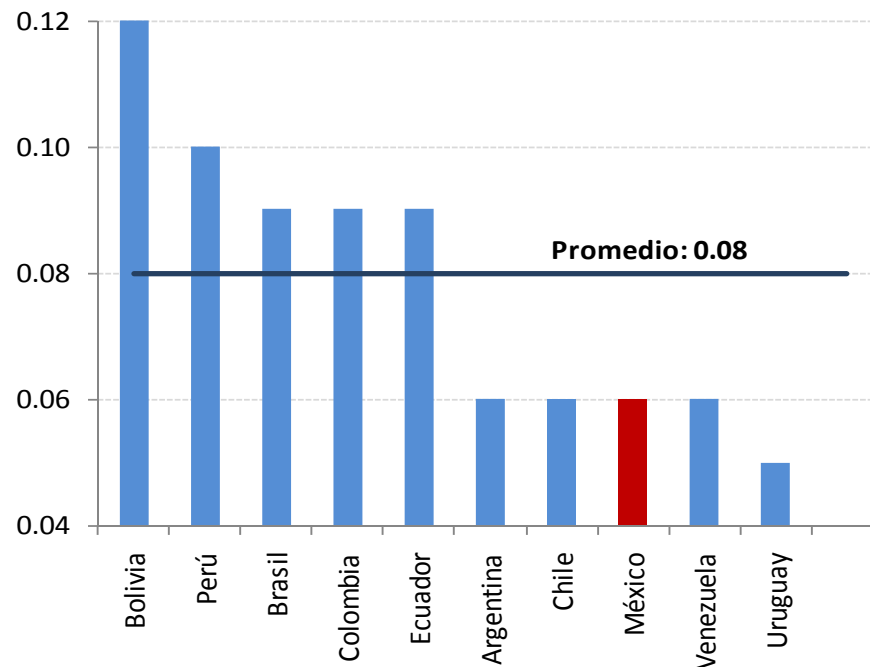
# Infrastructure, competitiveness and development

- The challenge is closing the gap in infrastructure with South East Asian economies. This would boost growth and reduce inequality

Potential GDP growth rate increase if infrastructure is similar to South East Asian economies (percentage points)



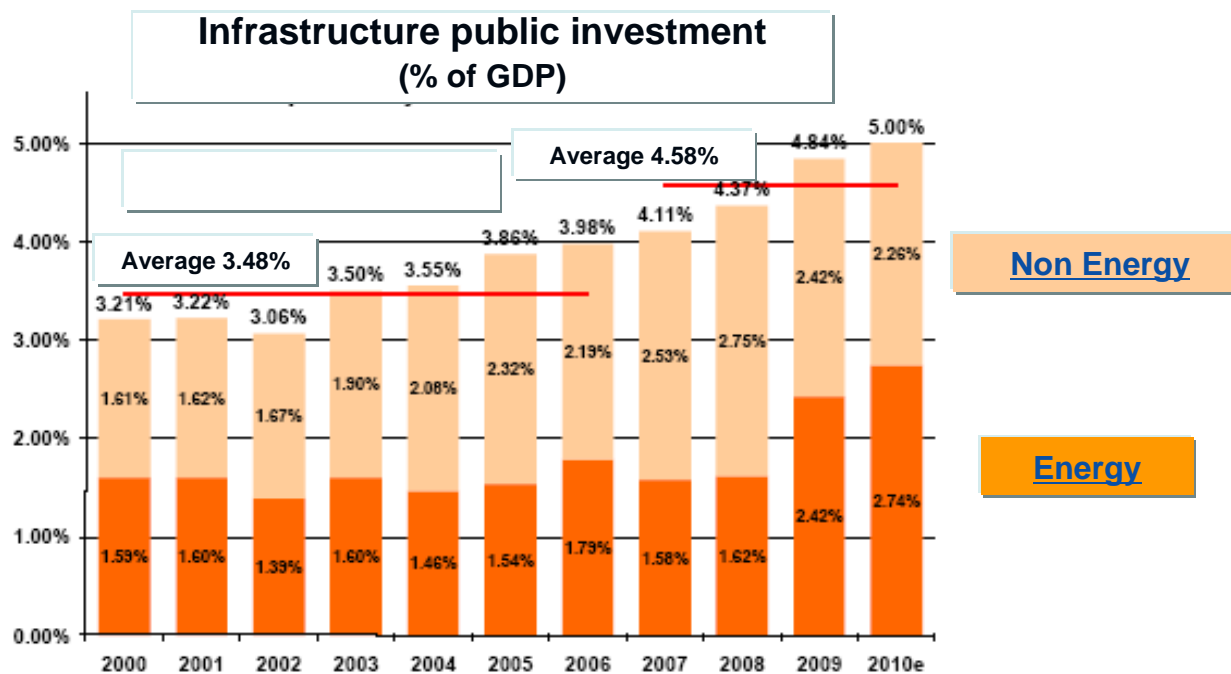
Gini index reduction in infrastructure is similar to South East Asian economies (Absolute values)





# Mexican actions to fostering infrastructure

- Design and development of a National plan for promoting infrastructure projects
- Promote new contracts and instruments. Thinking outside of the box
- Goal: 2030 México should be in the top 30
- 50 % of resources have been allocated to energy projects



Source: SHCP



# .. Public plan make possible PPP's

- Looking for private funding - non oil sectors
- Bank loans, debt issuance (prefered and subordinated) and capital risk
- Private resources should account for almost 60% of the National plan for promoting infrastructure projects (excluding energy and oil)

Infrastructure National Project (billions of dollars)		
	2007-2012	Advance %
Sector	26.5	10.8
Highways & Roads	4.5	2.0
Railroads	6.6	1.9
Airports	5.5	0.8
Telecommunications	26.1	7.8
Water & Environmental	18.6	7.7
<b>Subtotal</b>	<b>87.8</b>	<b>35.0</b>
Electricity	35.1	34.0
Oil	110.8	46.0
<b>Total</b>	<b>233.7</b>	<b>40.0</b>

Private  
&  
Public  
Investment

Public  
Investment

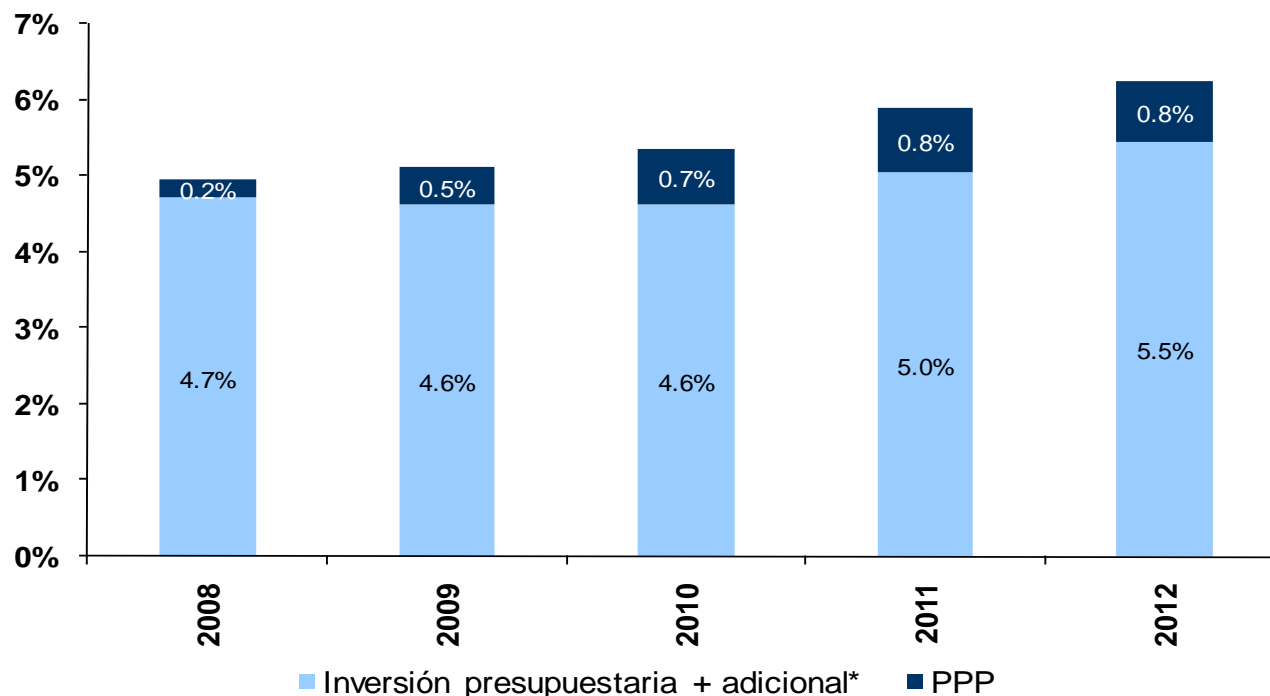




# .. Public plan make possible PPP's

- The New regulatory framework (Law APP) should promote higher funding from private sector and bolster public - private alliances

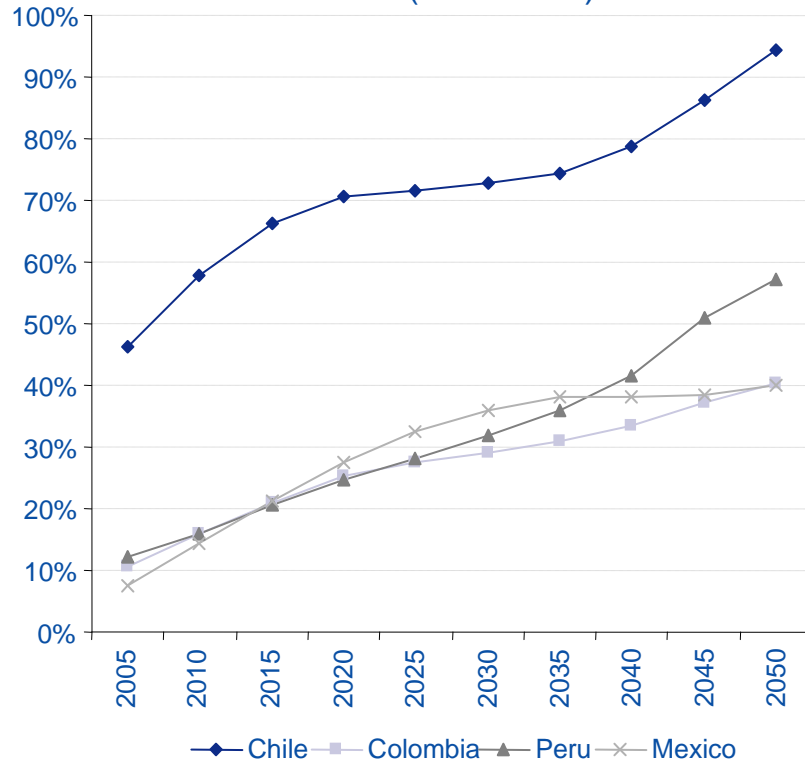
Investment expenditure in infrastructure  
(% of GDP)



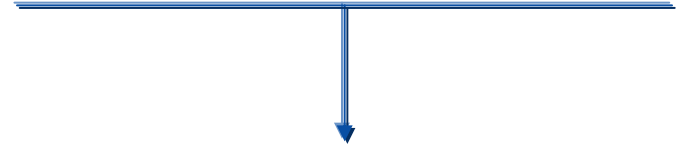
Source: SHCP

# Pension Funds, a natural funding source for infrastructure

Pension Funds Portfolio  
(% of GDP)



Pension funds in the region will accumulate a considerable stock of savings in the following decades



Pension funds will be the main source of funding for infrastructure projects

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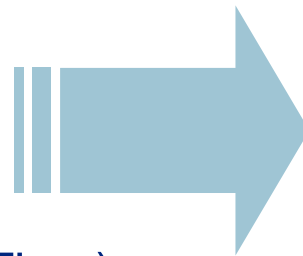
# The future on economic relationships: location and geographic advantages

LATAM should exploit its geographical proximity to the US market and competitive advantages to attract China's FDI; **thus Mexico can become a not obvious winner in this relationship**

Closeness

Transport costs

Inventories (Just in Time)



Complementary schemes

FDI

Intra-industry trade

Add value (complementary schemes)

In order to attract FDI, Latin American countries still has much work to do in improving their institutions and infrastructure

Latin America is and will continue to be an important market for China/HK (export diversification and provision of services).

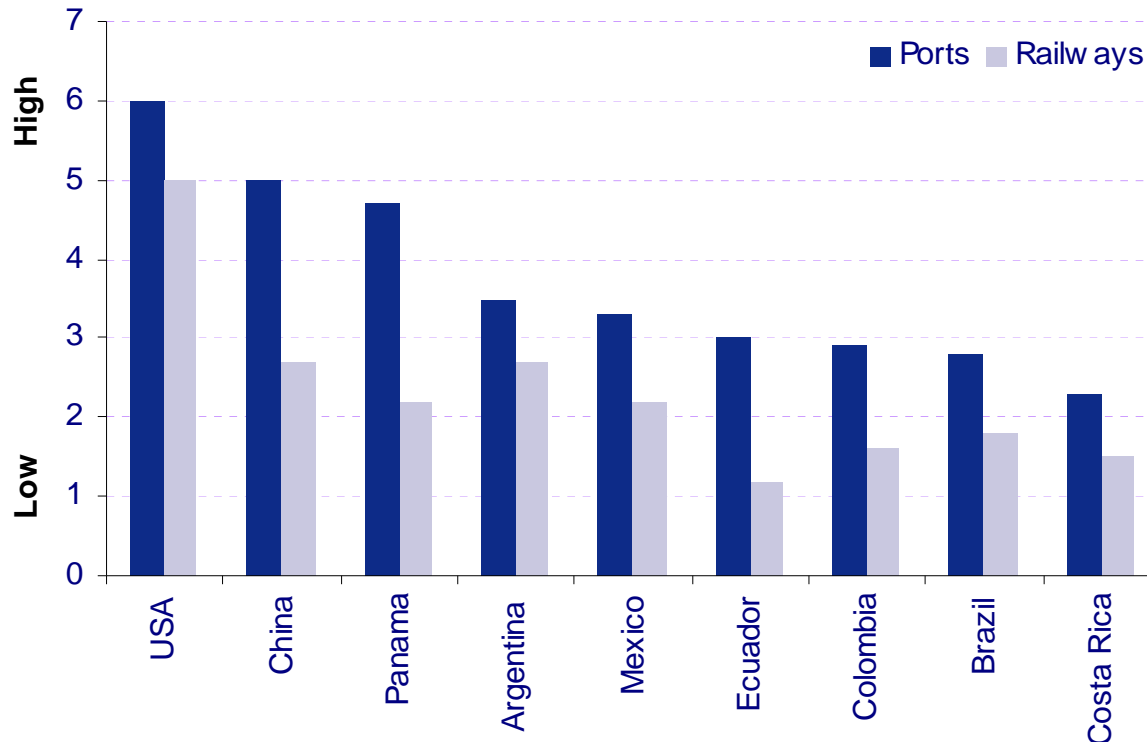


# The future on economic relationships: Challenges for becoming a key partner

**The challenge for LATAM is to identify sectors and products where distance and time are key competitive assets.** In order to capitalize on these sectors improvements on infrastructure should come first

## Infrastructure for Trade in Latin America

Source: OECD Development Centre, 2008, based on CGLA Infrastructure Database on Global Infrastructure Competitiveness (2006) and World Economic Forum (2005) data



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## Although there are challenges Mexico is a great opportunity within Latam

- **Its macroeconomic situation is among the soundest**
- **It is less dependent on Asia and, thus, a better diversification of risks**
- **Infrastructure projects are huge and interesting enough**
- **Mexico should take advantage of its geographic location. Becoming a hub for Chinese FDI is the easiest way to be part of the new value chain.**

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