

Macroeconomic Research
Macro Scenario – Mexico
August 2024

MEXICO: policy challenges amid lower rates

1. Lower rates this year

- Our end of year policy rate stands at 10.00%, which implies 25-bp cuts in each remaining policy meeting this year

2. Institutional deterioration?

- A constitutional reform to the judicial system that could reduce its independence is in the spotlight

3. U.S. Election spillovers

- China's presence in Mexico's trade flows, migration, and drug cartels are likely to be hot topics in the U.S. election

4. Nearshoring

- Will positive benefits from nearshoring show more clearly in activity data this year?

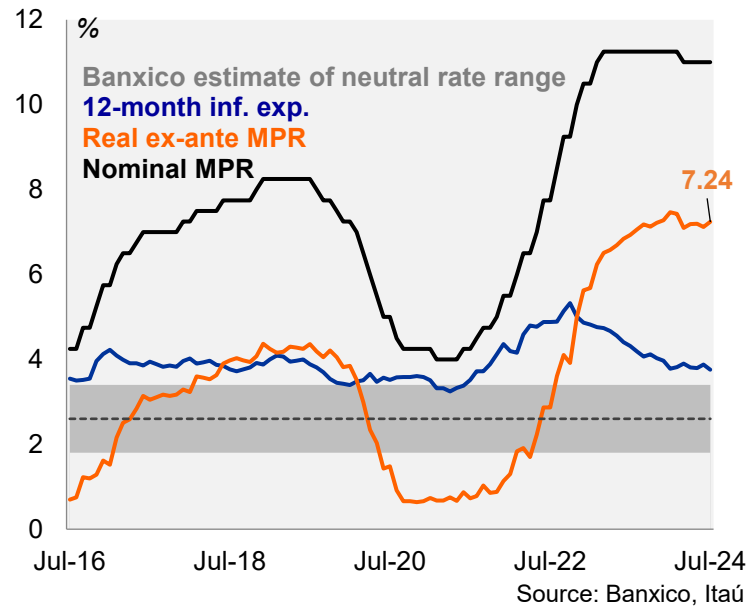
5. Challenging fiscal consolidation in 2025

- Spending pressure from social programs poses challenges to fiscal consolidation³.

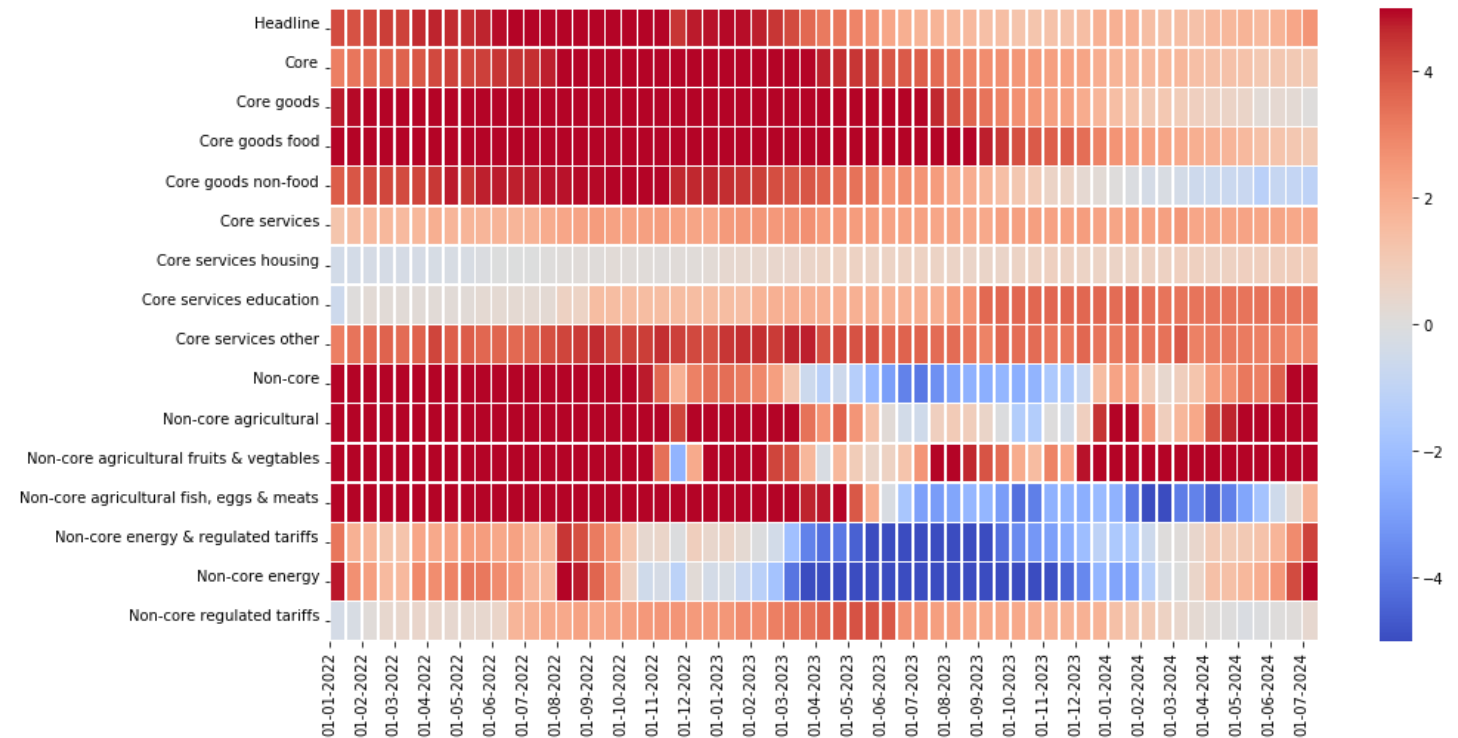
1. Lower rates this year

Lower inflation gap amid very tight monetary policy opens room for rate cuts this year

Measures of interest rates



Annual Inflation Heat Map, relative to Banxico target

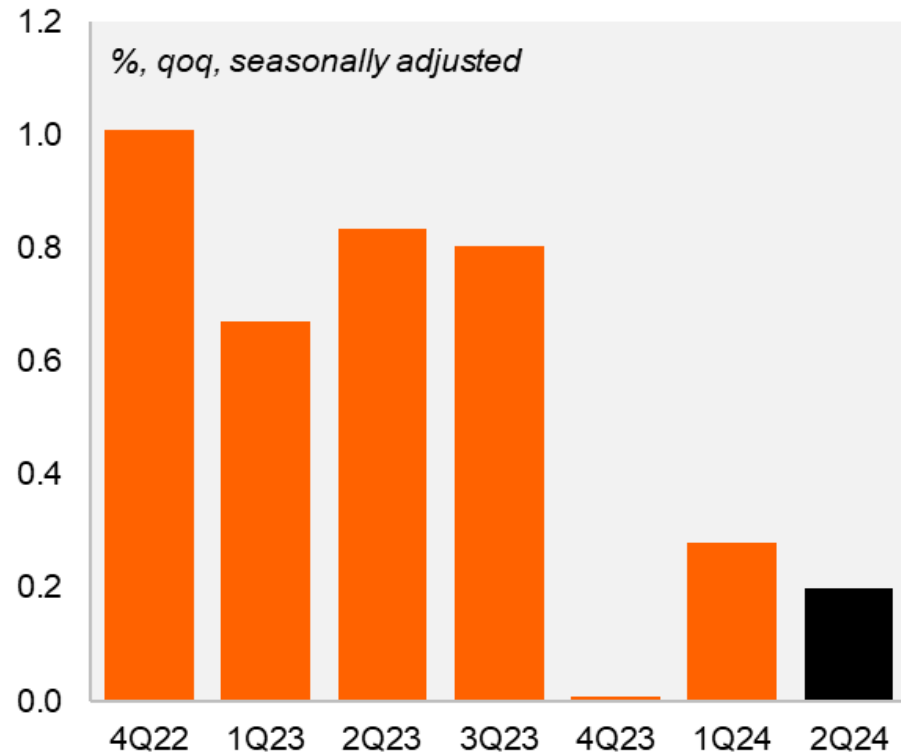


Source: INEGI, Itaú.

1. Lower rates this year

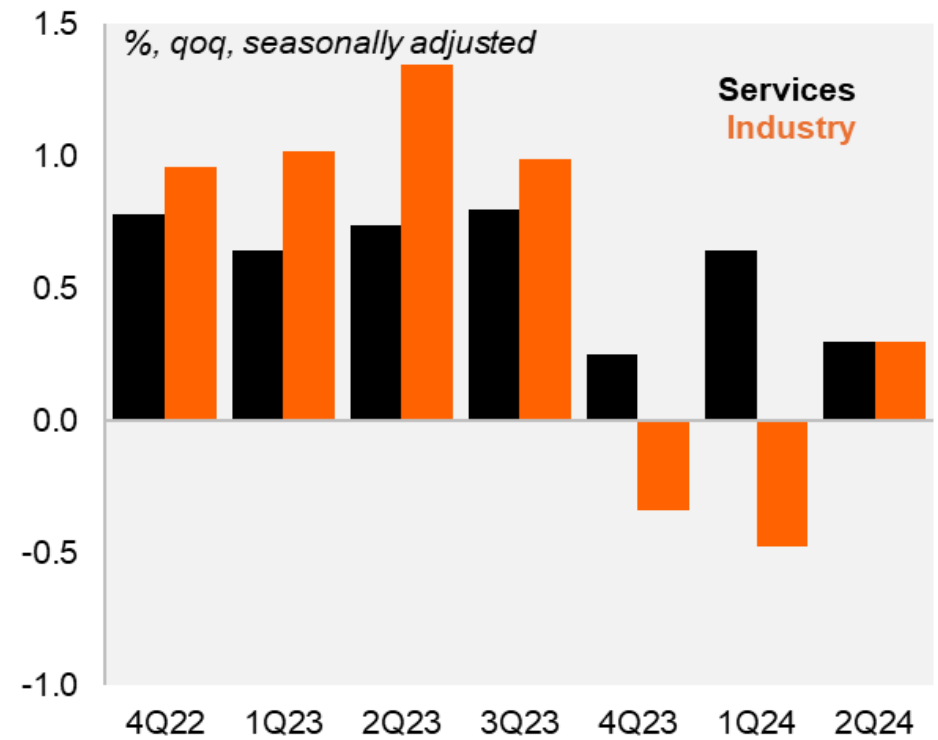
A weaker activity outlook also supports rate cuts during the rest of the year

Another soft GDP expansion in 2Q24



Source: INEGI, Itaú

Industrial and services sectors were also soft



Source: INEGI, Itaú

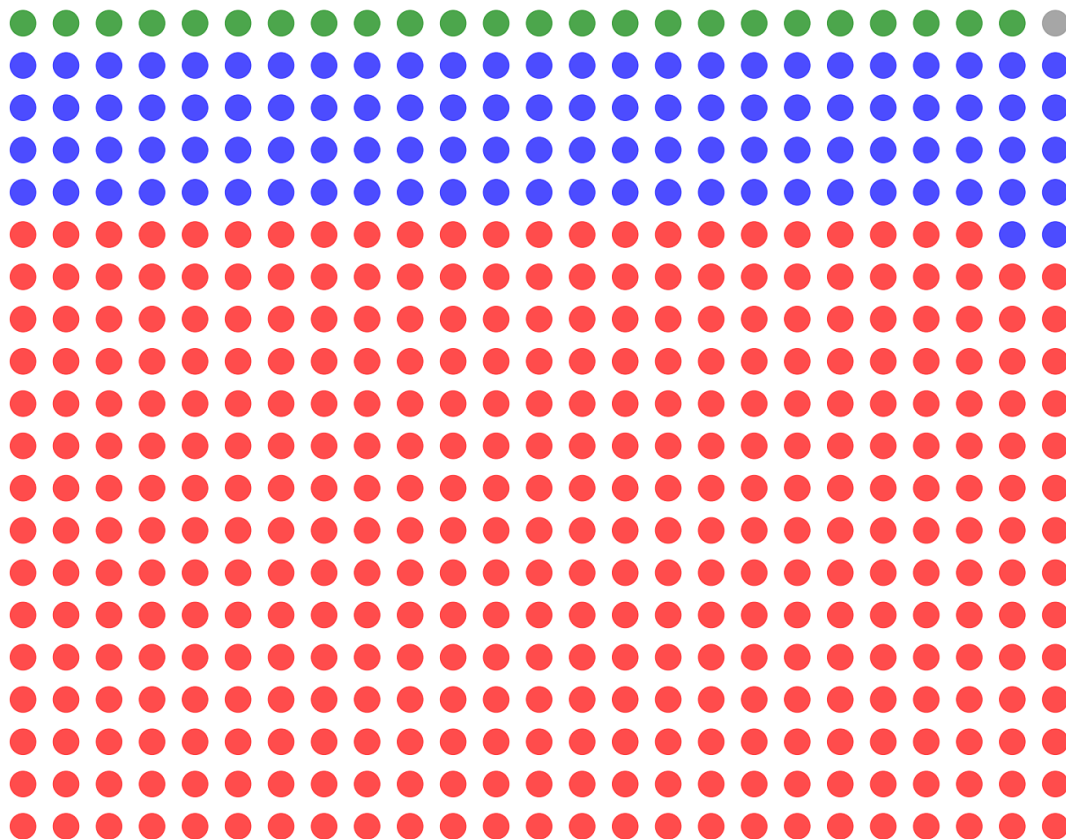
2. Institutional deterioration?

The incumbent's significant majority in Congress facilitates constitutional reform.

Preliminary Lower chamber composition*

Number of seats

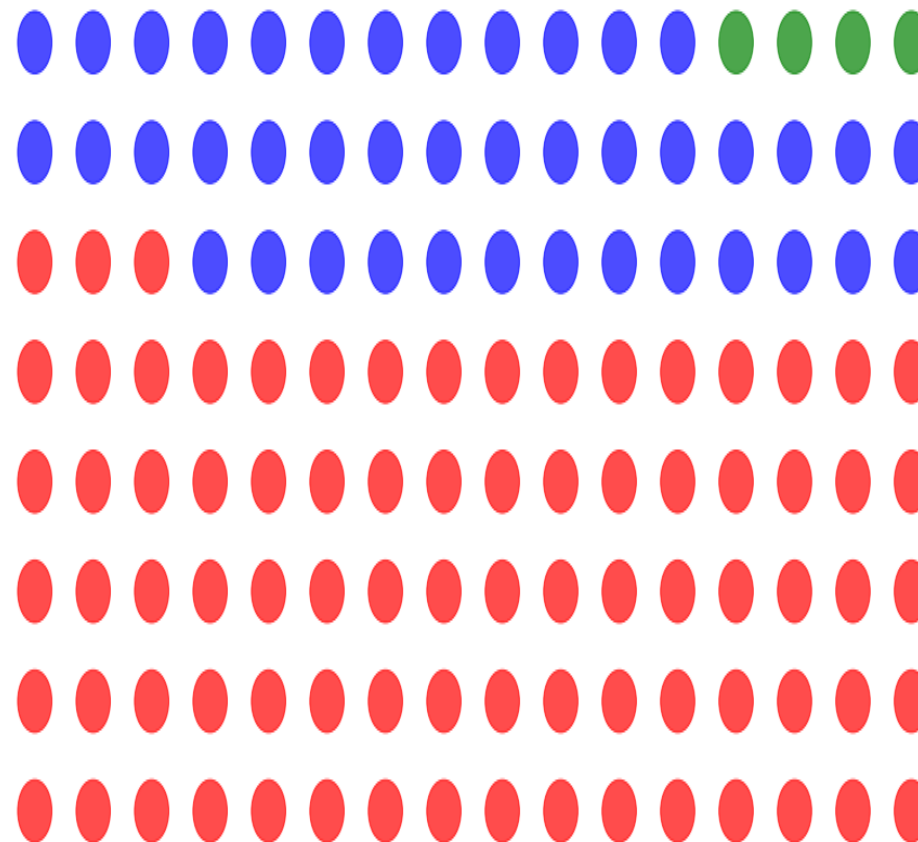
Morena & coalition: 373 (75%)
Opposition coalition: 102 (20%)
MC: 23 (4.8%)
Independent: 1 (0.2%)



Preliminary Senate composition*

Number of seats

Morena & coalition: 83 (65%)
Opposition coalition: 41 (32%)
MC: 4 (3%)



*Electoral authority (INE) will publish the final composition of Congress around mid August.

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2. Institutional deterioration?

A constitutional reform to the judicial system that could reduce its independence has been in the spotlight

The constitutional reform to the judiciary is expected to be submitted to the new Congress in early September.

Main points of the reform:

- **Popular election of supreme court justices, district judges and the electoral court in 2025** (more than 1,600 positions).
- Candidates would be proposed by the executive, legislative and judicial powers.
- The reform would also reduce the number of members of the Supreme Court from eleven to nine and revise their terms down from 15 to 12 years.
- **Separately, the reform limits the power of judges by forbidding them to suspend legislations, regulations or decrees while justices analyze if there is a violation of constitutional rights.**

2. Institutional deterioration?

An overview of Sheinbaum's campaign proposals

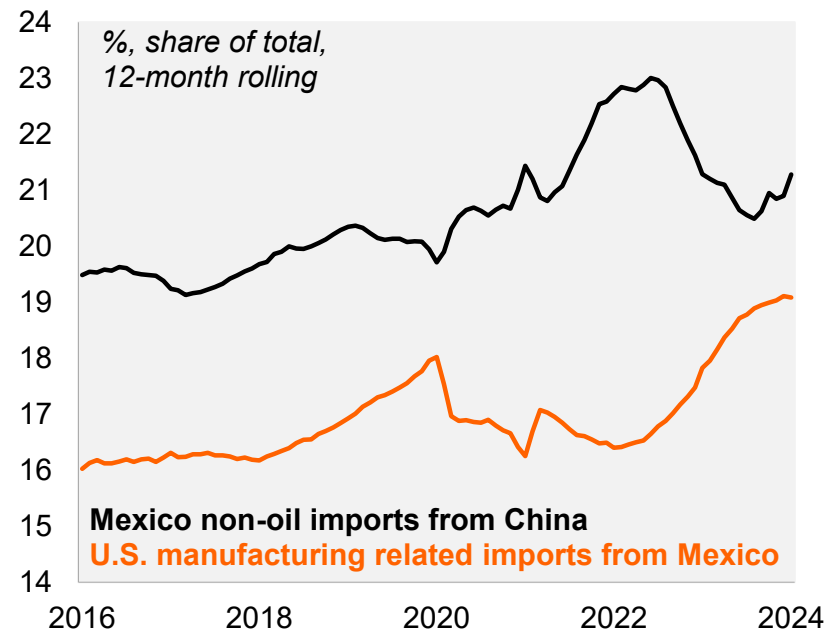
Proposals	Needs Congressional Approval		None
	Simple	Qualified	
Keep social programs of the current administration: pensions for persons with disabilities; job training programs for younger age groups; scholarships for low-income families; fertilizers support; support for small farmers ("Sembrando Vida"); guaranteeing prices for agricultural products (the government buys certain agricultural products when the prices are low).	To include them in the Budget	To include them as a right in the constitution.	
Subsidy to gasoline excise tax.	To include it in the Budget		
Freeze electricity tariffs in real terms.	To include it in the Budget		
Freeze gas prices in real terms.	To include it in the Budget		
Increases of the minimum wage at around an 11%. The proposal intends to take the minimum wage to 2.5 times a basic consumption basket.			
Temporary non-contributive pension (60-64) for women.	To include it in the Budget		
Supporting the development of renewable energies: photovoltaic, wind, hydraulic, geothermal plants, green hydrogen, the promotion of solar panels on the roofs of homes and businesses. However, the CFE (electricity public company) would keep the current market share of 54%.		To regulate the electricity market share.	
Nearshoring. Creation of development poles to foster investment throughout the country.	To include it in the Budget and secondary legislation.		
Pension reform. Increasing replacement rates. Formal workers under a defined contribution scheme will have the right to receive a pension equivalent to their last salary but limited to the current average salary of formal sector workers. A reform that would create a fund using unclaimed resources from pension-fund affiliates to finance the increase in replacement rates was already approved.	Changes to secondary legislation are sufficient.	However, AMLO intended these reforms at the constitutional level.	
Other pending AMLO's reforms. Establish a minimum salary (in line with average formal sector salaries) for teachers, police, soldiers, nurses and medics; forbidding GMO maize and fracking; lower spending on the electoral institute; forbidding open pit mining concessions; elimination of some autonomous organisms (not referring to the central bank) and regulators.	Most of them need only changes to secondary legislation.	Some of them need a Constitutional change.	

3. U.S. Election Spillovers

China's presence in Mexico's trade flows, migration, and drug cartels are likely to be hot topics in the U.S. election

- **USMCA's sunset provision:** In the summer of 2026, each country must agree to extend the agreement's term for 16-years. If any of the three decline, all Parties will have a joint review every year, for 10 years, in order to solve those elements that do not allow for the Agreement's extension. In the scenario of reaching year 16 without confirming the extension of the agreement, it would be concluded.

Trade indicators

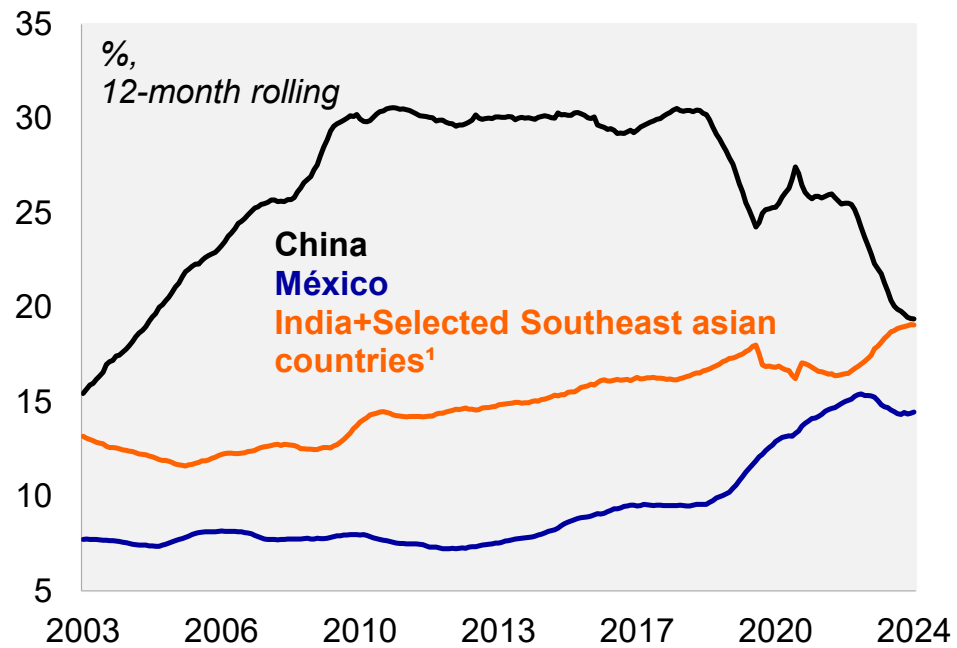


Source: U.S. Census Bureau, Banxico.

4. Nearshoring

Will the positive benefits from nearshoring show more clearly in activity data this year?

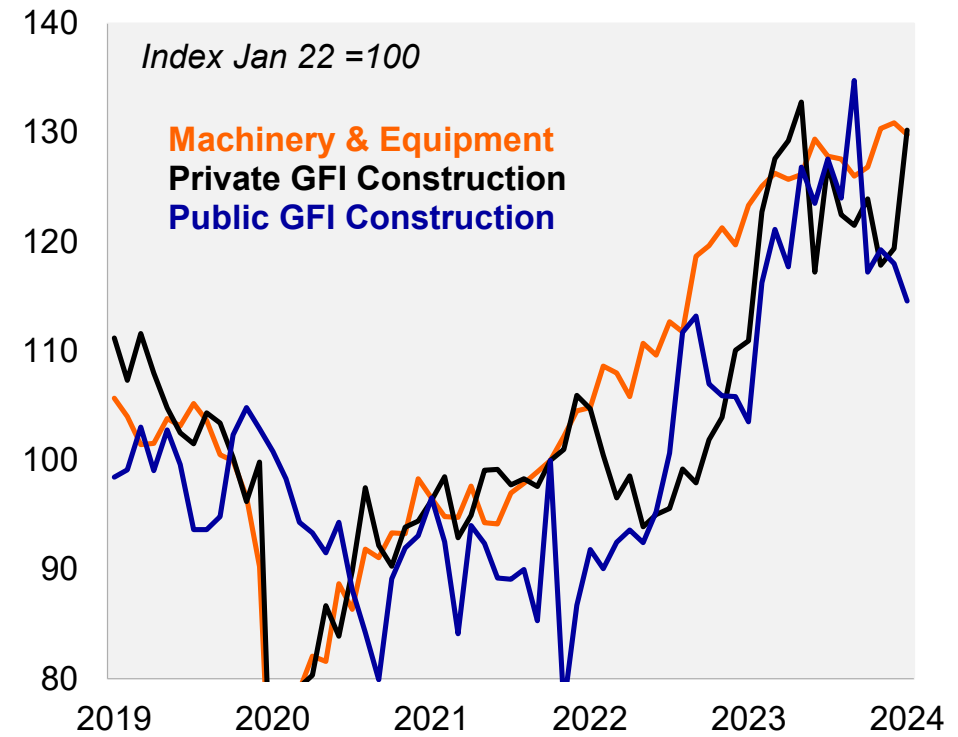
Share in U.S. manufacturing related imports by region



¹ Cambodia, Indonesia, Malaysia, Philippines, Thailand, Vietnam

Source: U.S. Census.

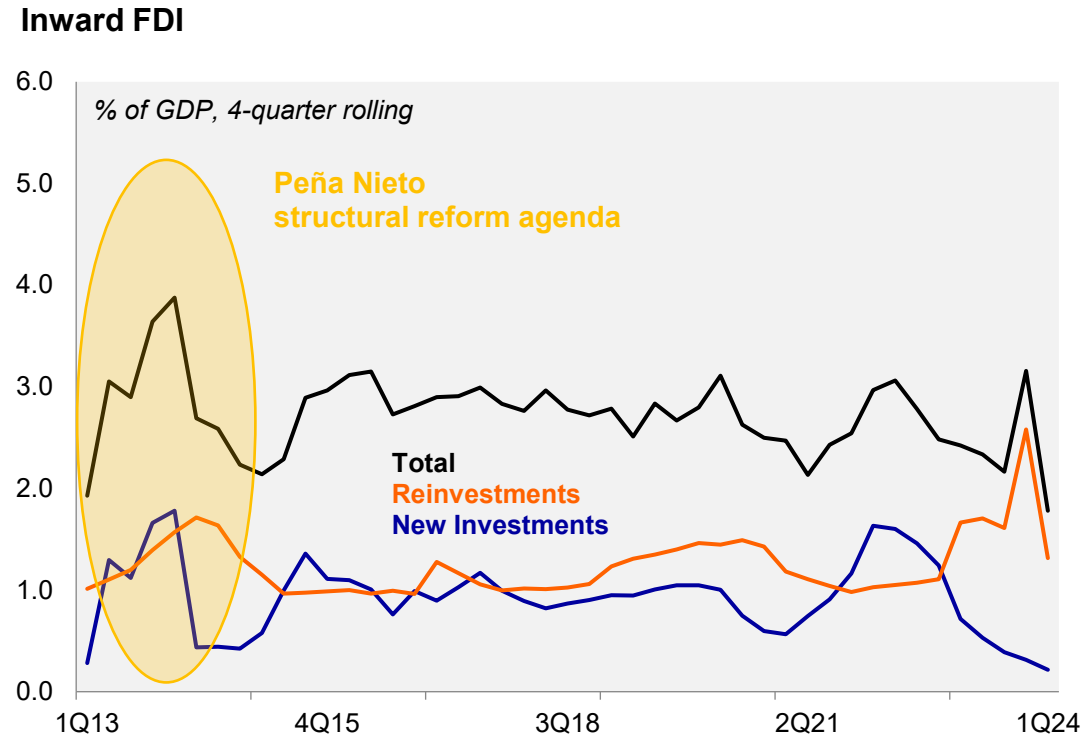
Strong GFI



Source: INEGI

4. Nearshoring

However, FDI, especially new investments, have not changed materially.



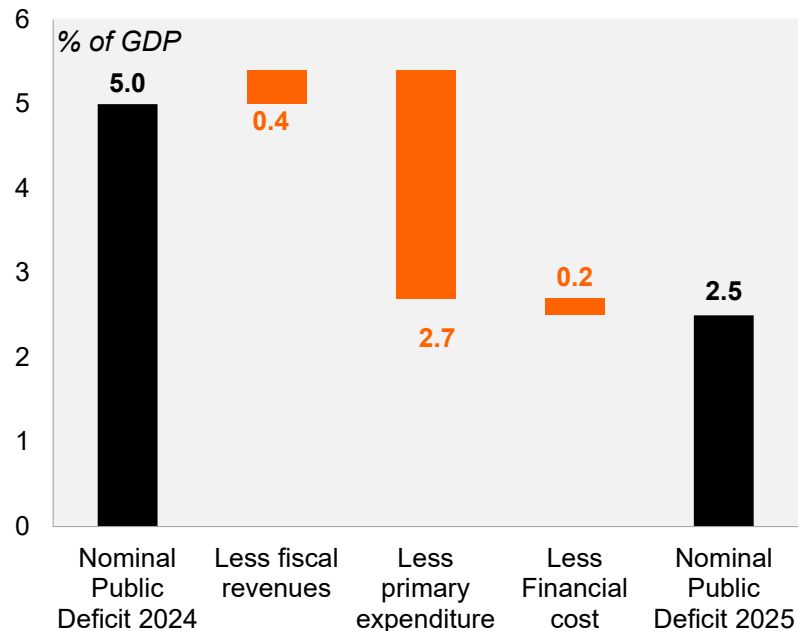
Source: Banxico.

5. Challenging fiscal consolidation for 2025

Spending pressure from social programs poses challenges to the fiscal consolidation process

- The 2025 fiscal budget will be presented to Congress by November 15, at the latest.

Challenging fiscal consolidation



Note: The chart shows official estimates from MoF's 2025 preliminary economic policy guidelines published last March. However, President elect Sheinbaum has signaled a slightly less ambitious fiscal consolidation reaching a nominal public deficit around 3.0% of GDP in 2025.

Social priority programs

	MXN Billion				
	2021	2022	2023	2024	2025
Total	333.5	450.3	600.3	741.5	860.0
Universal Pension (non-contributive)	135.1	238.0	335.5	465.0	483.0
Pension for persons with disabilities	15.5	18.0	24.1	27.9	28.9
Support for kids	2.7	2.8	2.9	3.1	3.2
Youngsters job training program	20.6	21.2	23.1	24.2	25.1
Guarantee Prices	11.0	11.4	12.0	12.5	13.0
Sembrando vida (support for small farmers)	28.9	29.4	37.1	38.9	40.4
Scholarships for low income families	75.3	82.6	83.6	87.7	92.7
Fishing support	1.5	1.6	1.7	1.8	1.8
Fertilizers	1.9	2.5	16.7	17.5	18.2
Schools	12.3	14.0	27.1	28.4	29.5
Agricultural production (support for small farmers)	13.5	14.0	15.5	16.3	16.9
Reconstruction	1.8	1.9	1.2	0.0	0.0
Urbanization improvement	4.1	4.2	6.6	4.4	4.6
Social housing	8.4	4.3	4.5	4.7	4.9
Public Universities	1.0	1.0	1.5	1.6	1.6
Purchase of Milk	0.0	3.3	7.2	7.5	7.8
Universal scholarship program ¹					34.0
Subsidies to women 60-64 years old ¹					54.4
				% of GDP	
<i>Total priority programs</i>	1.3	1.5	1.9	2.2	2.4
<i>Programs protected as a right in the constitution</i>	0.8	1.1	1.4	1.7	1.7
<i>Programs to be protected as a right in the constitution</i>	0.3	0.3	0.3	0.3	0.5
<i>New programs added by Sheinbaum</i>					0.2

Source: Criterios Generales de Política Económica 2021, 2022, 2023, 2024 y Pre-criterios 2025.

¹ Estimate.

Scenario Forecast

	2019	2020	2021	2022	2023	2024F		2025F	
						Current	Previous	Current	Previous
Economic Activity									
Real GDP growth - %	-0.4	-8.4	6.0	3.7	3.2	1.6	1.6	1.7	1.7
Nominal GDP - USD bn	1,298	1,129	1,318	1,463	1,794	1,946	1,949	1,936	1,937
Population (millions)	125.6	127.7	129.0	130.1	131.2	132.3	132.3	133.4	133.4
Per Capita GDP - USD	10,335	8,844	10,218	11,241	13,672	14,707	14,729	14,517	14,527
Unemployment Rate - year avg	3.5	4.4	4.1	3.3	2.8	2.7	2.7	2.7	2.7
Inflation									
CPI - %	2.8	3.2	7.4	7.8	4.7	4.3	4.3	3.9	3.9
Interest Rate									
Monetary Policy Rate - eop - %	7.25	4.25	5.50	10.50	11.25	10.00	10.00	8.00	8.00
Balance of Payments									
MXN / USD - eop	18.9	19.9	20.5	19.5	17.0	18.6	18.6	19.3	19.3
Trade Balance - USD bn	5.4	34.2	-10.8	-26.9	-5.5	-10.0	-10.0	-15.0	-15.0
Current Account - % GDP	-0.3	2.4	-0.3	-1.2	-0.3	-0.4	-0.4	-0.6	-0.6
Foreign Direct Investment - % GDP	2.3	2.8	2.7	2.7	1.7	3.0	3.0	3.5	3.5
International Reserves - USD bn	180.9	195.7	202.4	199.1	212.8	220.0	220.0	225.0	225.0
Public Finances									
Nominal Balance - % GDP	-1.6	-2.8	-2.8	-3.2	-3.3	-5.0	-5.0	-2.5	-2.5
Primary Balance - % GDP	1.1	0.1	-0.3	-0.4	-0.1	-1.4	-1.4	0.9	0.9
Net Public Debt - % GDP	43.9	49.9	48.9	47.6	46.8	50.2	50.2	50.6	50.6

Source: IMF, Bloomberg, INEGI, Banxico, Haver and Itaú

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