



## Outlook

	Average 10-14	2015	2016	2017	2018	2019	2020	2021	2022	Forecasts
GDP growth (%)	-1.5	3.3	2.6	2.1	2.2	-0.1	-8.2	4.0	2.5	
CPI Inflation (%)*	3.9	2.7	2.8	6.0	4.9	3.6	3.4	3.8	3.7	
Fiscal balance (% of GDP)	-3.9	-4.0	-2.8	-1.1	-2.2	-2.3	-5.8(e)	-3.4	-2.6	
Public debt (% of GDP)	44.4	52.8	56.7	54.0	53.6	53.7	65.5(e)	65.6	65.4	
Reference rate (%)*	4.1	3.0	4.2	6.7	7.6	8.1	5.5	3.6	3.8	
Exchange rate (MXN/USD)*	12.9	15.8	18.7	18.9	19.2	19.3	21.5	20.8	19.5	
Current balance (% of GDP)	-1.5	-2.7	-2.3	-1.8	-2.1	-0.3	1.2(e)	-0.1	-0.9	
External debt (% of GDP)	19.4	26.2	29.7	28.1	28.3	27.9	31.6(e)	32.5	33.1	

Notes: \* Annual average. (e): estimation.

Source: CaixaBank Research, based on data from national statistical agencies and the IMF.

- **Among Latin American countries, Mexico is one of the most affected by the COVID-19 shock and one of those with the lowest and most fragile growth prospects (+ 4.0% in 2021, compared to -8.2 % in 2020).** Thus, as a result of a rather lax anti-COVID health policy, the prevalence of the pandemic has been quite high, which has ended up causing significant economic disruption. The economic impact, unlike in other countries in the region, has not been partially offset by an ambitious economic policy response. Looking ahead, growth prospects are mainly based on the transfer of the US recovery to the Mexican foreign sector, since neither a greater economic policy focus nor a strong internal recovery is expected in view of the slow vaccination process. The fact that it is an election year complicates government decision-making. In this context, the risk balance is clearly trending downward.
- **Real shock of COVID-19.** The country's health strategy against COVID-19 has been somewhat lax and, therefore the level of incidence of the virus is high (at the time of writing this country outlook, Mexico is the third highest country in number of deaths globally, after the US and Brazil). Despite this permissive approach, which in principle should have allowed less of a decline in mobility and activity, it was not possible to prevent a large economic contraction from occurring in 2020 (the aforementioned -8.2%), being among the most severe in Latin America. Perhaps the key has been that, in the most productive sectors, rigorous self-isolation guidelines have been followed. Based on this situation, future health prospects are maybe less favourable than in other countries. In particular, the low vaccination uptake will complicate a rapid return to normality and critical areas such as tourism, may suffer if the country is not perceived as a safe destination, even if issuer markets (in particular, the US) recover.

### • Economic policy response

- **Fiscal policy.** Although nominally Mexico's fiscal position is not bad, dependence on Pemex and the lack of progress in reducing public debt (which is around 65.5% of GDP, closer to areas of risk than comfort) result in a de facto reduction of the fiscal room for manoeuvre. Given this situation, the Government has preferred not to risk its reputation as an orthodox country in terms of public finances and to date has only made tentative decisions to increase public expenditure. It is estimated that the Mexican fiscal impulse is one of the lowest in Latin America.

## Outlook (continued)

- **Monetary policy.** Banxico has dealt with the shock more proactively than the Government and has responded by reducing the interest rate by 325 bp (to 4.0%) since the start of the pandemic. In addition, a series of liquidity support measures have been adopted for banks (in particular, by expanding the range of eligible collateral instruments and including development banks in a liquidity facility), guaranteeing the good performance of bonds and facilitating the flow of credit to Mexican micro, small and medium-sized firms. In general terms, the solvency and liquidity situation of the large banks is reasonably favourable, but there is concern about the impact that the increase in non-performing loans will have on other less solid entities, especially as loan moratoria expire, being an instrument widely used to respond to the shock.
- **Evolution of the exchange rate.** The combination of the macroeconomic impact, the increase in sovereign risk and a half-hearted economic response since the beginning of the COVID-19 shock have resulted in the peso depreciating against the dollar by more than 10%. Looking ahead, the great uncertainty surrounding Mexico's economic and financial situation leads us to believe that the downward pressure on the peso will continue.

## Main risks

The risk balance is clearly trending downward. Specifically, there are several categories:

- **Macroeconomic.** The main risk is that the US recovery will be slower or less vigorous than anticipated. A second risk is that the expected modest oil recovery will not take place (a more important situation because of its consequences for Pemex than because of the growth itself).
- **Political.** To date, the Government, to a greater or lesser extent, has balanced its different sensitivities: mixing the somewhat more orthodox and business-friendly approach with others that could be characterised as more unorthodox. In particular, the main elements of non-intervention in the productive economy have been respected (with the exception of the energy sector, central in the government agenda), safeguarding the independence of Banxico (it is significant that the threat to force the purchase of dollars has been slowed), orthodoxy in fiscal matters and maintenance of economic integration with the United States. However, after the foreseeable revalidation of support for the Government expected in the legislative, state and local elections, there are doubts as to whether this balance will remain present in the second part of the legislature. What is less likely, unfortunately, is that the structural reforms with a greater impact on the economic future will be accelerated. In particular, the much-needed tax reform seems essential to obtain greater revenues and thus be able to finance pressing infrastructure investment needs.
- **Sovereign.** The main risk is that a bail-out will arise through recapitalisation, writing-off of Pemex's debt and/or reduction of the fiscal revenues required of Pemex, which would cause an increase in Mexico's public deficit and debt. Likewise, it cannot be ruled out that if there was an increase in the aforementioned perception of political risk, in the sense of moving away from the balance between orthodoxy and heterodoxy, there could be increased sovereign risk. For now, even if the risks mentioned do not arise, we consider that, according to macro fundamentals, a drop of around one notch in 2021 in the credit rating cannot be ruled out.

	Rating	Last changed	Outlook	Last changed
STANDARD &POOR'S	BBB	26/03/20	Negative	01/03/19
Moody's	Baa1	17/04/20	Negative	05/06/19
FitchRatings	BBB-	15/04/20	Stable	15/04/20

■ Indicates that the country is rated as "investment grade".

□ Indicates that the country is not rated as "investment grade".

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