Contents

1 Structural features

2 Recent developments and outlook

3 Inflation and monetary policy

4 Economic challenges
Mexico has a large and well-diversified economy

- 11th largest economy\(^1\)
- Middle-income country, US$14,610 per capita\(^1\)
- Population of 112.3 million, more than half under the age of 25
- Economy oriented to services: 65% of GDP and 62% of the labor force
- 30% of GDP and 24% of the labor force in industrial activities
- High openness to foreign trade and investment

\(^1\) Based on PPP-adjusted GDP

Note: Data is for 2011, except for population, which is for 2010
Source: IMF, April 2012 World Economic Outlook Databases and INEGI
Opening to trade and investment has resulted in highly dynamic export industries

<table>
<thead>
<tr>
<th>World Rankings for Selected Mexican Exports</th>
<th>Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Railway cars</td>
<td>1</td>
</tr>
<tr>
<td>Beer</td>
<td>1</td>
</tr>
<tr>
<td>Motor vehicles for the transport of goods</td>
<td>2</td>
</tr>
<tr>
<td>Refrigerators and freezers</td>
<td>2</td>
</tr>
<tr>
<td>Television receivers</td>
<td>2</td>
</tr>
<tr>
<td>Tractors</td>
<td>3</td>
</tr>
<tr>
<td>Parts for spark-ignition-type engines</td>
<td>4</td>
</tr>
<tr>
<td>Reinsurance services</td>
<td>4</td>
</tr>
<tr>
<td>Electric motors and generators</td>
<td>5</td>
</tr>
<tr>
<td>Motor cars for the transport of persons</td>
<td>9</td>
</tr>
</tbody>
</table>

Note: Data for 2011, except Reinsurance services, which is for 2010
Source: Trade Map, International Trade Centre
The functioning of the economy is based on solid macroeconomic fundamentals, including contained public debt.

**General Government Gross Debt**

<table>
<thead>
<tr>
<th>Year</th>
<th>Mexico</th>
<th>U.S.</th>
<th>Euro area</th>
</tr>
</thead>
<tbody>
<tr>
<td>1996</td>
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<td>1997</td>
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<tr>
<td>2011</td>
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</tr>
</tbody>
</table>

1/ Includes Federal Government, public enterprises, states and municipalities

Source: IMF

**Average Maturity of Federal Government Securities**

<table>
<thead>
<tr>
<th>Year</th>
<th>Mexico</th>
<th>U.S.</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
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<td>2001</td>
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<td>2010</td>
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<tr>
<td>2011</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2012</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

2/ Denominated in local currency

Source: Banco de México and US Treasury
... relatively low inflation and interest rates

**Annual Inflation**

- Mexico
- OECD

**Interest Rate**

1/ 28-day Cetes

Source: Banco de México

Source: OECD
... and a well-capitalized, provisioned and liquid banking system

<table>
<thead>
<tr>
<th>Banking System Indicators</th>
<th>2Q12</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Net Capital</strong> (% of risk-weighted assets)</td>
<td>15.94</td>
</tr>
<tr>
<td><strong>Tier 1 capital</strong> (% of net capital)</td>
<td>88.94</td>
</tr>
<tr>
<td><strong>Past-due loans</strong> (% of total loans)</td>
<td>2.50</td>
</tr>
<tr>
<td><strong>Provisions for expected losses</strong> (% of past-due loans)</td>
<td>186.50</td>
</tr>
<tr>
<td><strong>Liquid assets</strong> (% of net cash outflows)</td>
<td>338.60</td>
</tr>
</tbody>
</table>

*/ Calculations based on Basel III liquidity coverage ratio
Source: CNBV and Banco de México
The credibility of economic policy has fostered the development of financial markets

- The Mexican peso operates 24 hours and it is the most traded currency in emerging markets
- Two-thirds of Mexican peso trading is conducted by non-residents
- The domestic yield curve includes maturities of up to 30 years
- Approximately half of total outstanding peso-denominated government securities are held by foreign investors
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1. Structural features
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Since 3Q09, Mexico has shown a continuous process of economic recovery

Global Economic Activity
2003=100; s.a.

Industrial Production¹
2007=100; s.a.

s. a. / seasonally adjusted
Source: INEGI

¹ The correlation of industrial production between the two countries is close to 0.9
Source: INEGI
... driven by both external and internal demand

Manufacturing Exports by Destination
2007=100; s.a.

- Total
- U.S.
- Rest of the world

Retail Sales and Investment
2007 = 100; s.a.

- Retail sales
- Investment

s.a. / Seasonally and trend-adjusted
Source: Banco de México

s.a. / Seasonally and trend-adjusted
Source: Commercial establishment survey and Mexico’s National Accounts System, INEGI
Economic growth momentum has been accompanied by an improvement in labor conditions

Formal Private Sector Employment\(^1\)

Unemployment and Labor Force Participation\(^2\)

1/ Workers insured by the Mexican Social Security Institute (IMSS)
Source: IMSS

s.a. / Seasonally adjusted
2/ Unemployed people relative to Economically Active Population (EAP) and the EAP relative to those 14 and older, respectively
Source: INEGI

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... as well as financing to the private sector

Total Financing to the Non-Financial Private Sector

% of total; June 2012

Corporate 57.3%

Consumer 42.7%

Annual real growth, %

1/ Includes foreign financing, and domestic financing from commercial banks, development banks and non-bank financial intermediaries
Source: Banco de México
Mexico has also attracted an increasing proportion of capital inflows directed to emerging markets.

**Foreign Holdings of Peso Government Bonds**

% of Local Government Bonds held by Foreigners in EM¹

1/ Include Brazil, Hungary, India, Indonesia, Malaysia, Mexico, Poland, Thailand and Turkey

Source: Barclays

**Yield Curve**

%

1/ day  1/ month  3/ months  6/ months  1/ year  5/ years  7/ years  10/ years  20/ years  30/ years

* / September 14, 2012

Source: Banco de México

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14
Consensus forecasts posit Mexico's continued moderate growth for the near term

### GDP Outlook

<table>
<thead>
<tr>
<th></th>
<th>2011</th>
<th>2012&lt;sup&gt;F&lt;/sup&gt;</th>
<th>2013&lt;sup&gt;F&lt;/sup&gt;</th>
</tr>
</thead>
<tbody>
<tr>
<td>World</td>
<td>3.1</td>
<td>2.6</td>
<td>2.8</td>
</tr>
<tr>
<td>United States</td>
<td>1.8</td>
<td>2.2</td>
<td>2.1</td>
</tr>
<tr>
<td>Euro zone</td>
<td>1.5</td>
<td>-0.5</td>
<td>0.2</td>
</tr>
<tr>
<td>China</td>
<td>9.2</td>
<td>7.9</td>
<td>8.3</td>
</tr>
<tr>
<td>Brazil</td>
<td>2.7</td>
<td>1.8</td>
<td>4.0</td>
</tr>
<tr>
<td>Mexico</td>
<td>3.9</td>
<td>3.8</td>
<td>3.5</td>
</tr>
</tbody>
</table>

<sup>F</sup> Forecast

*Source: Consensus Forecasts, September 2012; and Latin America Consensus Forecasts and Asia Consensus Forecasts, August 2012*
The most important risks for Mexico’s economic scenario come from the United States and Europe

Risks

United States
- The “Fiscal Cliff” could lead to a fall of 0.3% for GDP in 2013\(^1\)
- As industrial production in the U.S. slows, the impact on the Mexican economy could be significant\(^2\)

Europe
- The difficulty resolving underlying problems could generate new bouts of volatility and risk aversion

\(^1\) Congressional Budget Office (2012) “An Update to the Budget and Economic Outlook: Fiscal Years 2012 to 2022”, August
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1 Structural features
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4 Economic challenges
Since mid-2011, inflation has been gradually increasing

Consumer Price Index

Annual; %

Source: INEGI

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... which reflects some exchange rate pass-through and pressures from food and agricultural prices

- Gradual increase in core inflation
  - Pass-through from peso depreciation in tradable goods

- Higher food and agricultural product prices that could last longer than expected
  - Drought
  - Bird flu outbreak in Mexico
Monetary policy will have to be adjusted in a timely way if convergence of inflation to the 3% target is endangered.

**Risks**

- Second-round effects of supply shocks
- Further FX volatility
- Rising demand pressures

✓ Some signs of slack have disappeared

→ Possible deterioration of inflation expectations
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1 Structural features
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4 Economic challenges
The task of macroeconomic stability is continuous and needs to be consolidated

- Fiscal reform
  - The efficiency of public revenues
  - Stabilization funds
  - Expenditures focused on public goods, e.g., security and infrastructure

- Convergence to inflation target

- Enhanced regulatory and supervisory framework of the financial system
  - Basel-principle-based rules for capitalization and liquidity
  - Macroprudential supervision
Furthermore, Mexico could increase its growth potential if barriers to total factor productivity are reduced

- Given their size in the economy, significant opportunities for productivity enhancement arise in services and non-manufacturing industries
- Key elements behind lagging productivity
  - Insufficient competition in crucial economic areas
  - Widespread informality
  - Education and skill gaps

Conclusions

- Mexico has a large and well-diversified economy
- The economic recovery is driven by both external and internal demand
- Expected moderate near-term growth is threatened by U.S. economic uncertainty and strains in global financial markets due to persistent problems in Europe
- Since mid-2011, inflation has been gradually increasing, reflecting foreign exchange rate pass-through and pressures from agricultural prices
- Monetary policy will have to be adjusted in a timely way if convergence of inflation to the 3% target is endangered
Mejoran las perspectivas económicas mundiales