

Ministry of Finance and Public Credit



Mexico: Economic Developments and Public Finances

Mexico's Day NASDAQ

July 31st, 2009

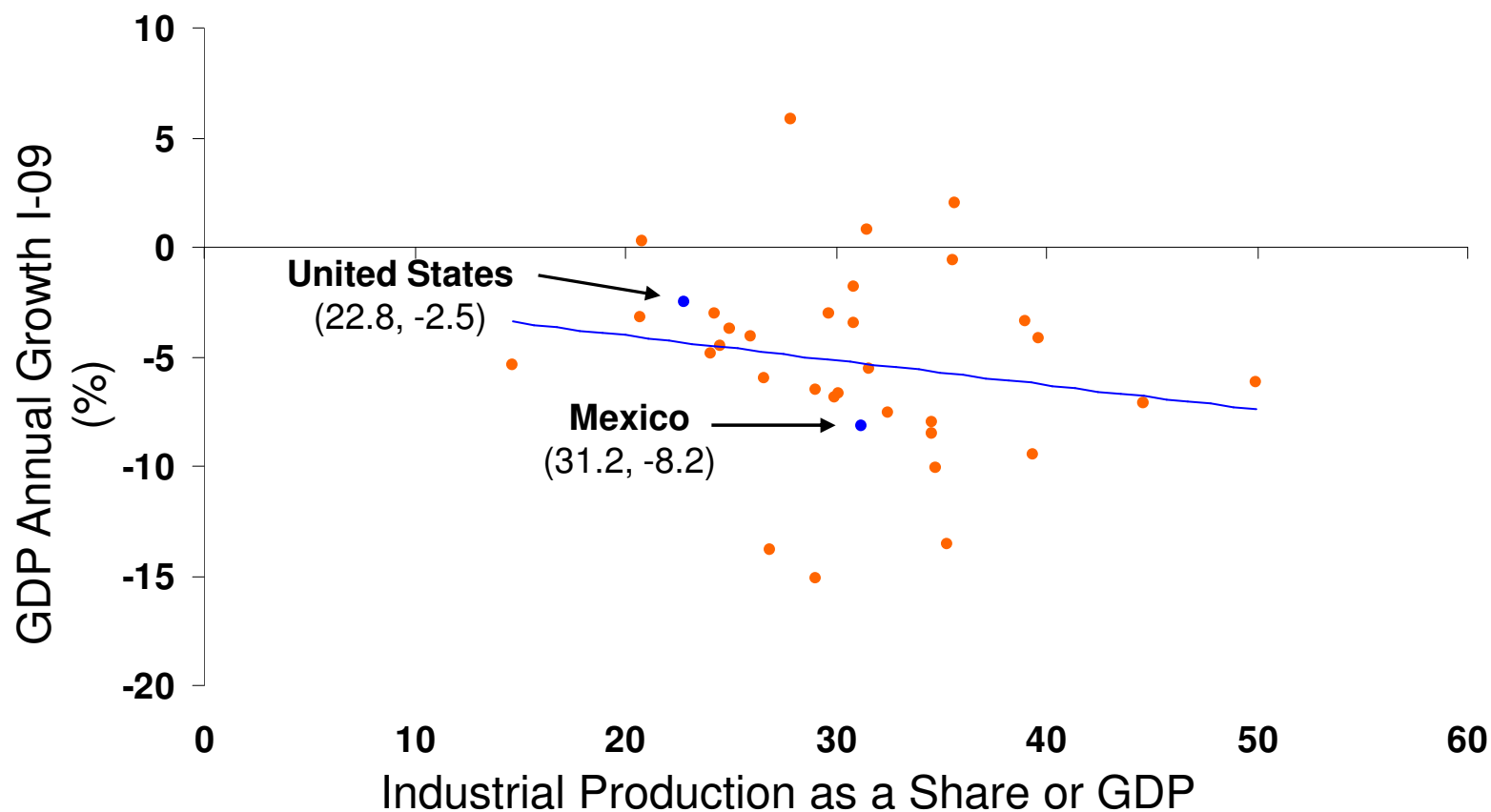
- 1. Current Economic Trends and Expected Recovery.**
- 2. Current Account Analysis.**
- 3. Fiscal Adjustment and Medium Term Fiscal Strategy.**
- 4. Factors Contributing to the Recovery.**

The decrease in economic activity during the end of 2008 and the first quarter of 2009 was higher in Mexico than in other countries because of the following:

- Production in Mexico is intensive in durable manufactured goods, with this sector being the most affected by the current global crisis.
- Mexico is one of the countries with the largest exposure to the United States through trade, tourism and investment. Moreover, GM and Chrysler had a large share of automobile production.
- The temporary effect of the influenza outbreak.
- The contraction of credit card loans which started even before the current slowdown.

GDP has fallen more for those countries with a higher share of industrial production in GDP.

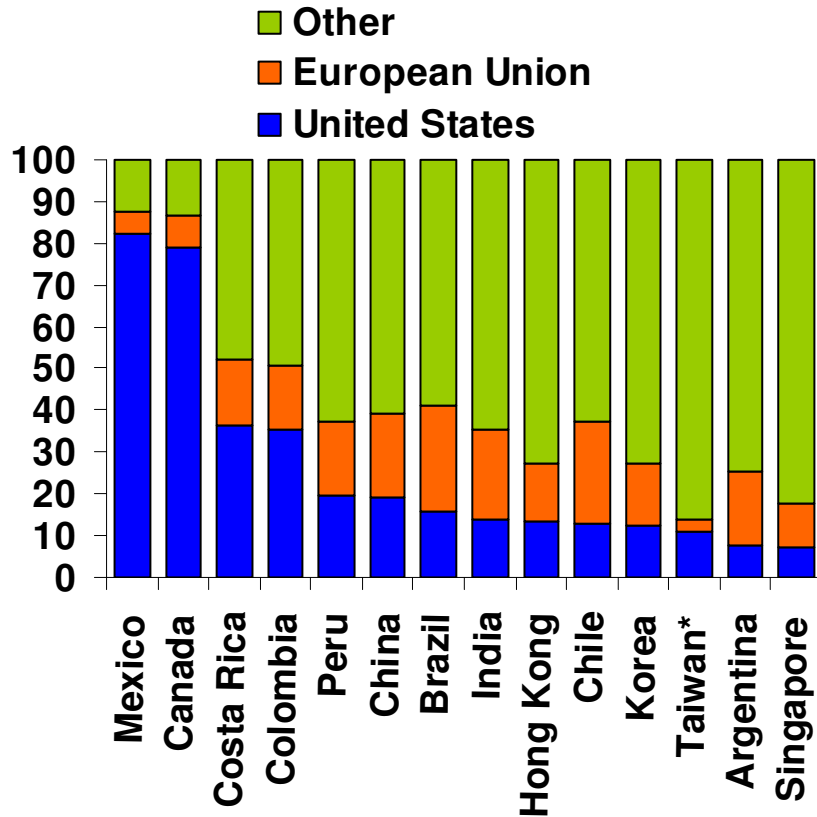
Industrial Production 2006 and Annual Growth I-09 (%)



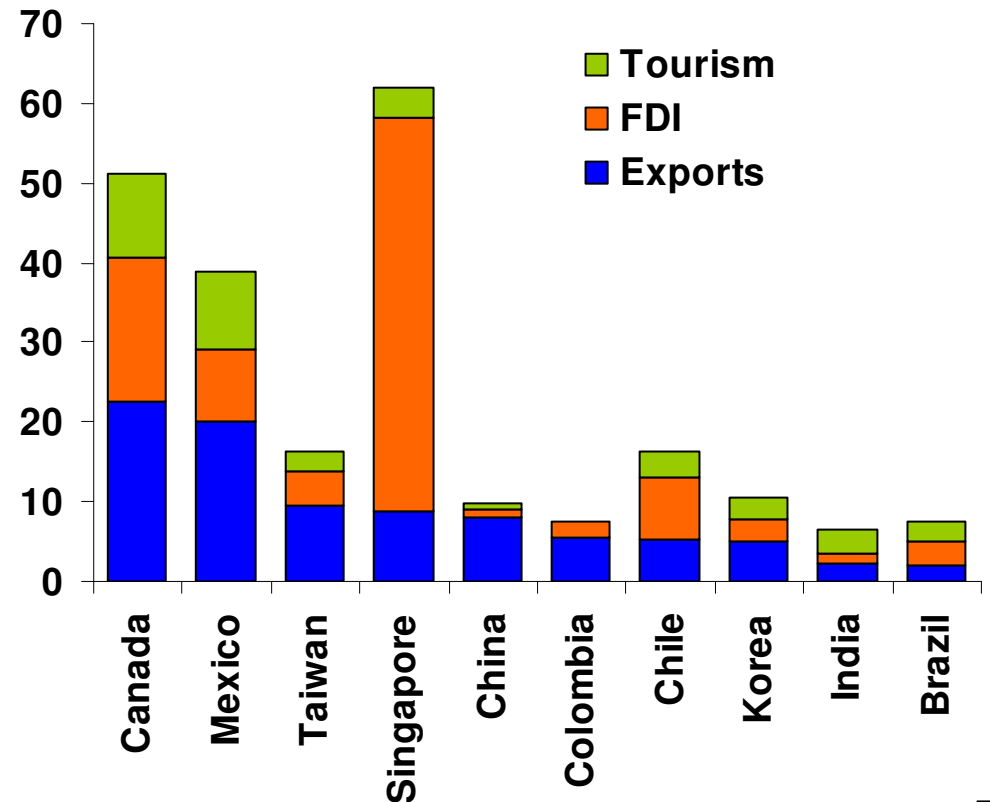


Mexico is particularly exposed to the US slowdown given its trade links and also through other channels such as tourism and FDI.

Main Trading Partners, 2008
(% of total exports)



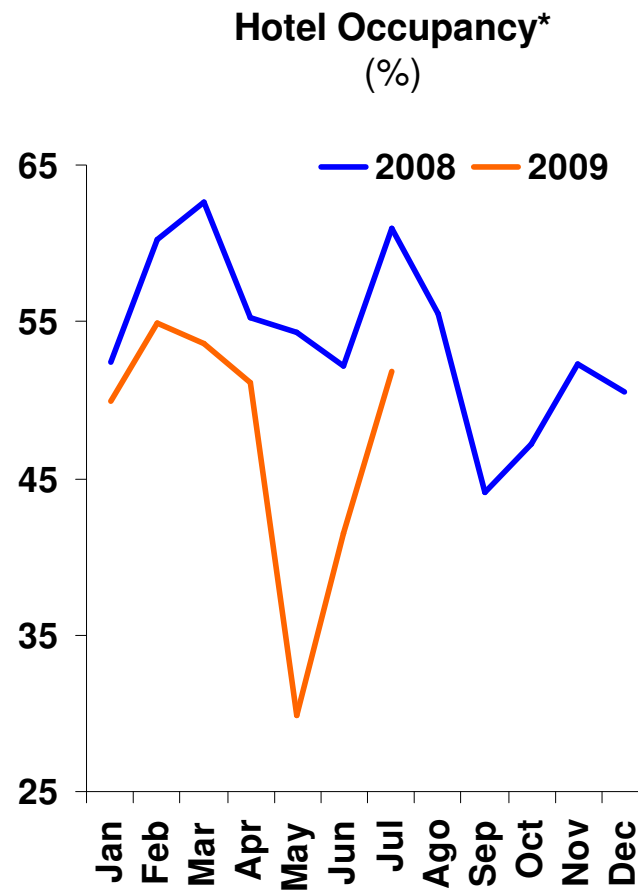
Non-Financial Flows from United States
(% of GDP of each country)



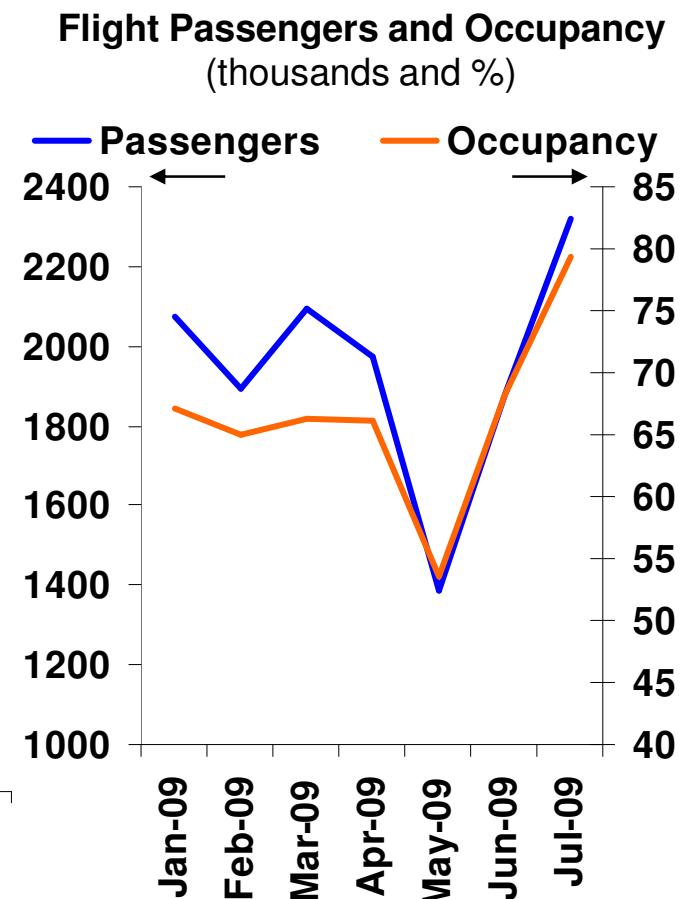
*Data for 2007, for the European Union only Germany, United Kingdom and Italy included

The influenza episode is expected to have reduced annual growth by 0.3%. Employment, hotel occupancy rates and air traffic indicate that a substantial recovery from the effects of the influenza was already underway in June.

	Employment (monthly change, workers)		
	Apr-09	May-09	Jun-09
Baja Calif. Sur	-612	-2215	-760
Distrito Federal	-3850	-8254	1610
Edo. México	-4818	-3849	2252
Guerrero	-28	-3269	1065
Oaxaca	34	53	2120
Quintana Roo	-2179	-21583	3521



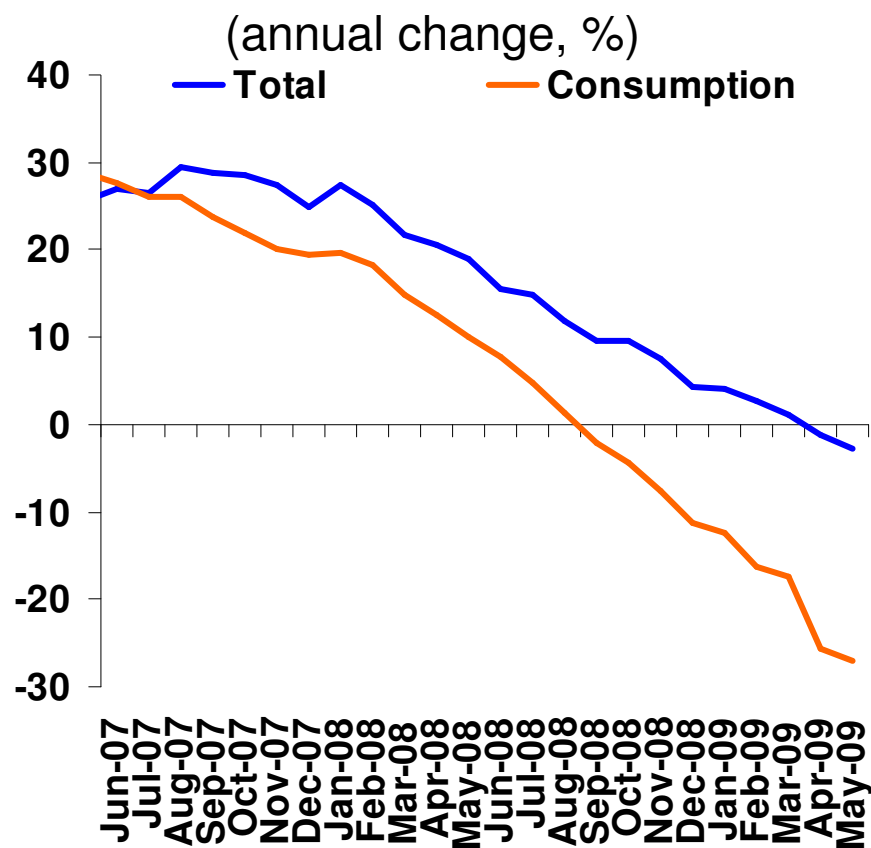
Source: Sectur
*Preliminary data for June 2009; data for July as of the second week of the month.



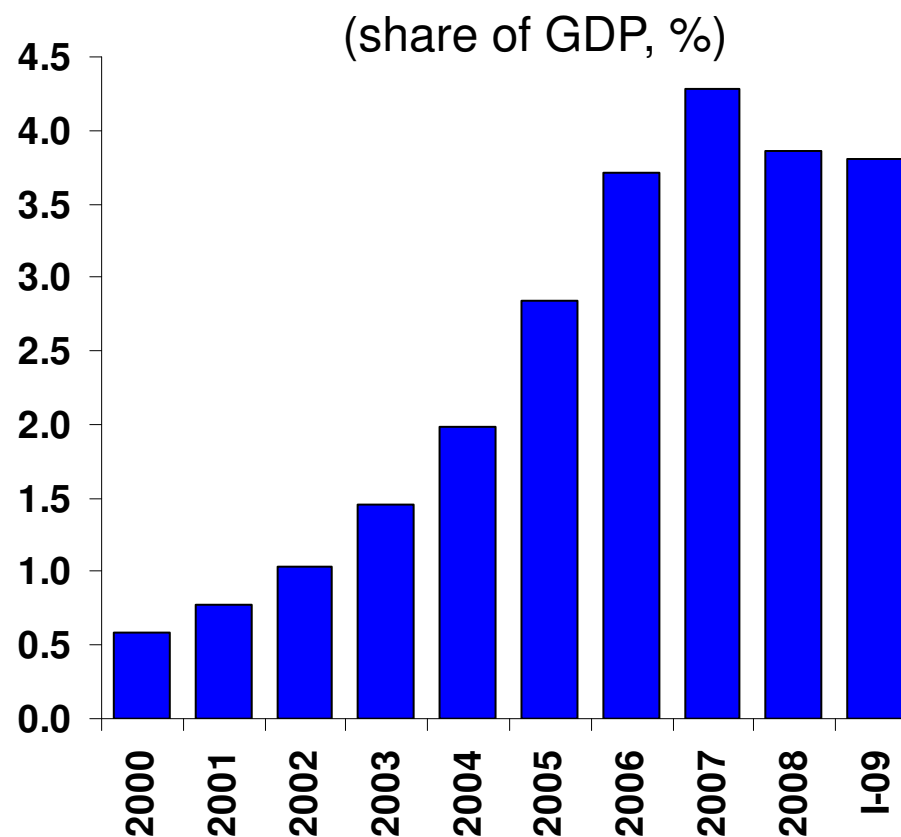
Data for Interjet, Mexicana, Aeromexico and Aeromar.

The deceleration in credit for consumption started before the recession as a response to increasing NPLs.

Credit from Commercial Banks to the Private Sector

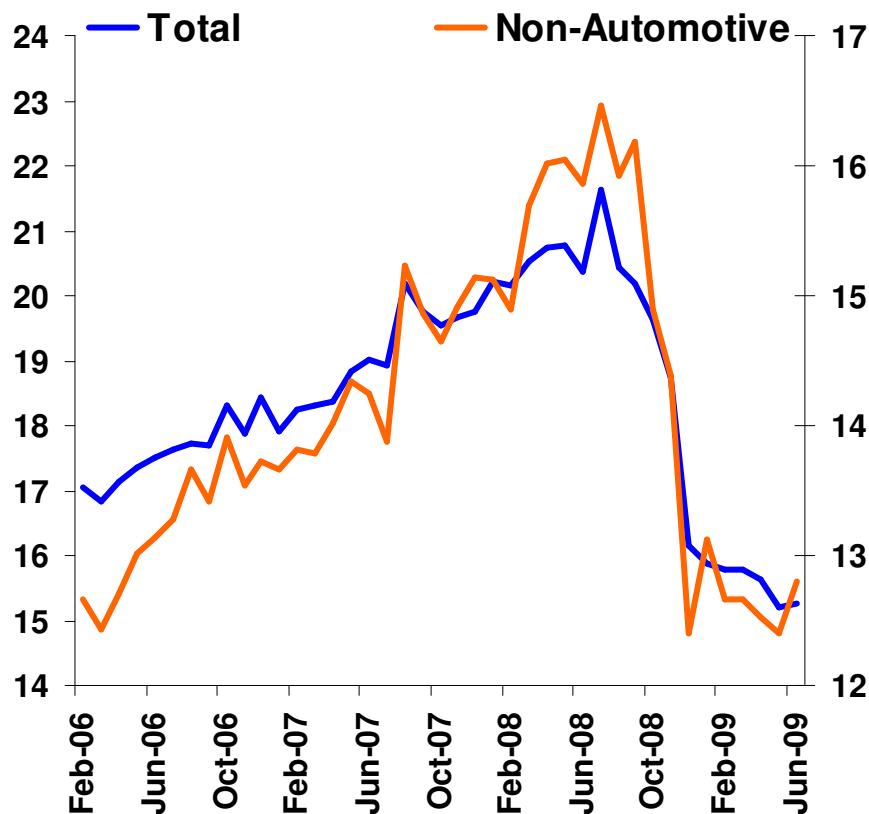


Consumption Credit from Commercial Banks



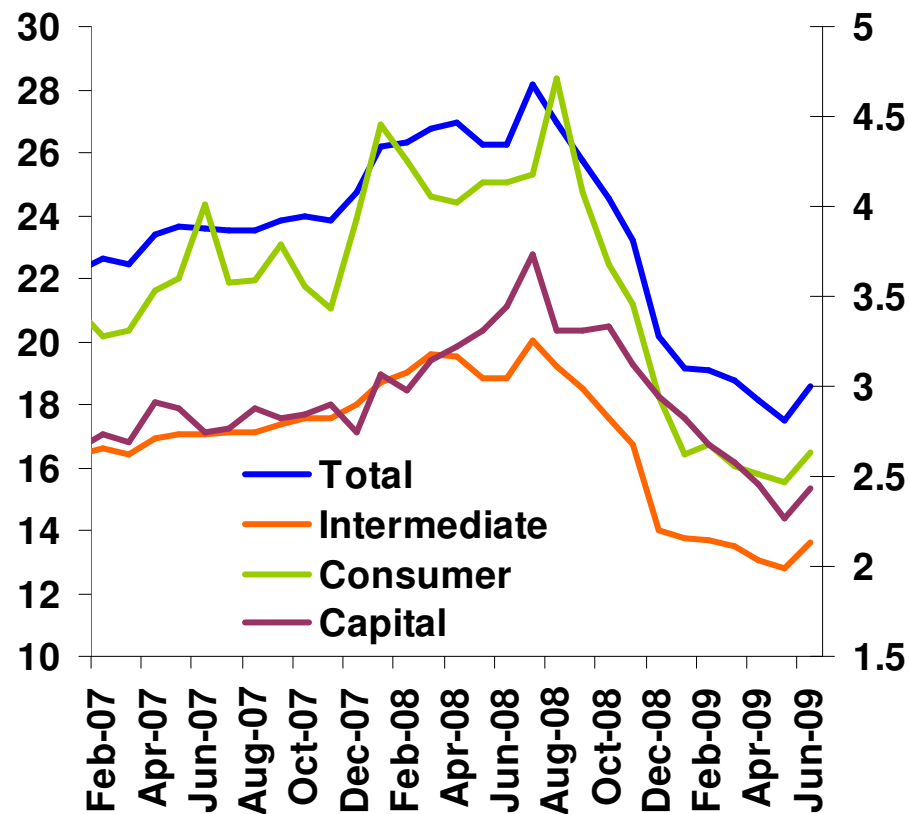
Given a contraction of 10% in the first half of 2009, market forecasts are consistent with a significant recovery in the second half of 2009. In June, a slight improvement was observed in both exports and imports, as the negative effect of the influenza episode receded.

Non-Oil Exports, SA
(billion dollars)



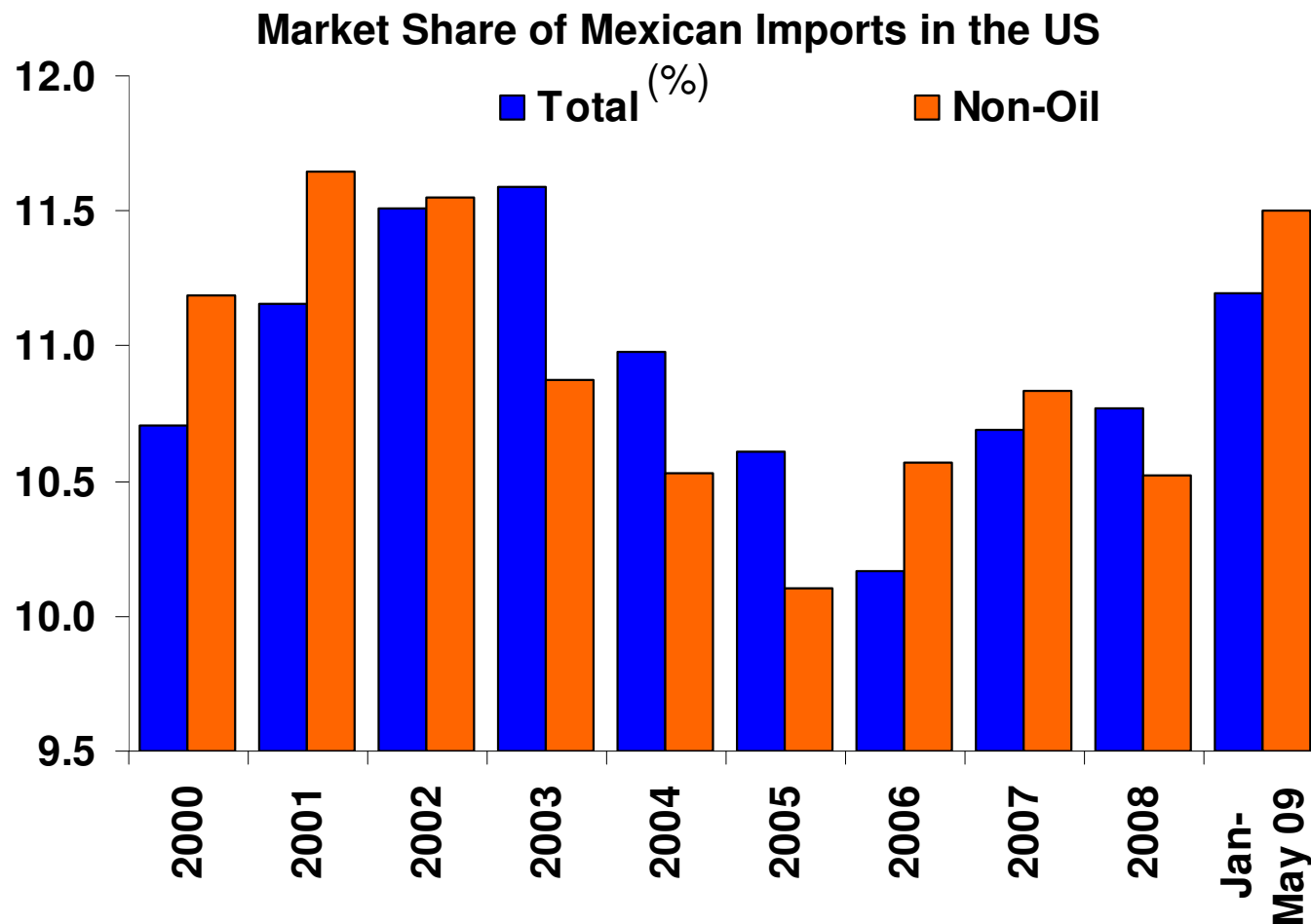
Source: INEGI

Total Imports, SA
(billion dollars)



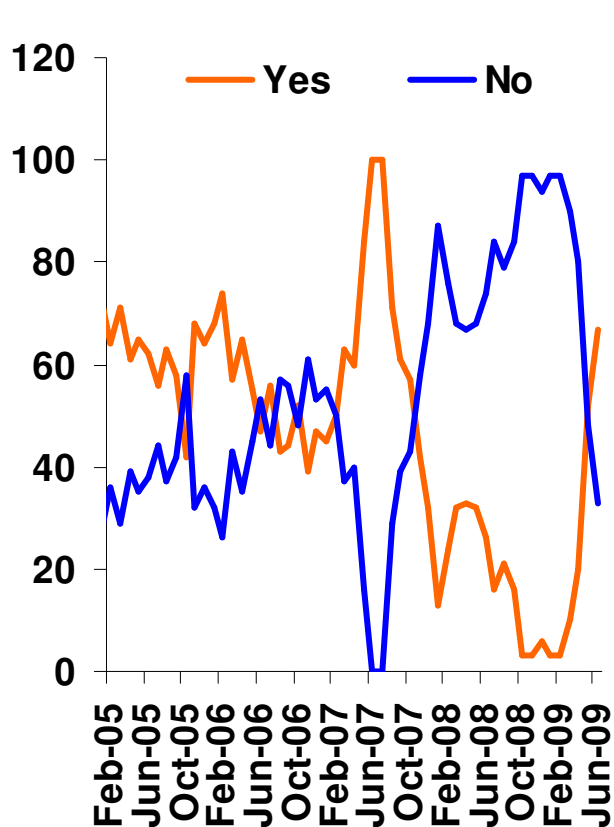
Source: INEGI

In addition, Mexico has been gaining significant market share in the US.



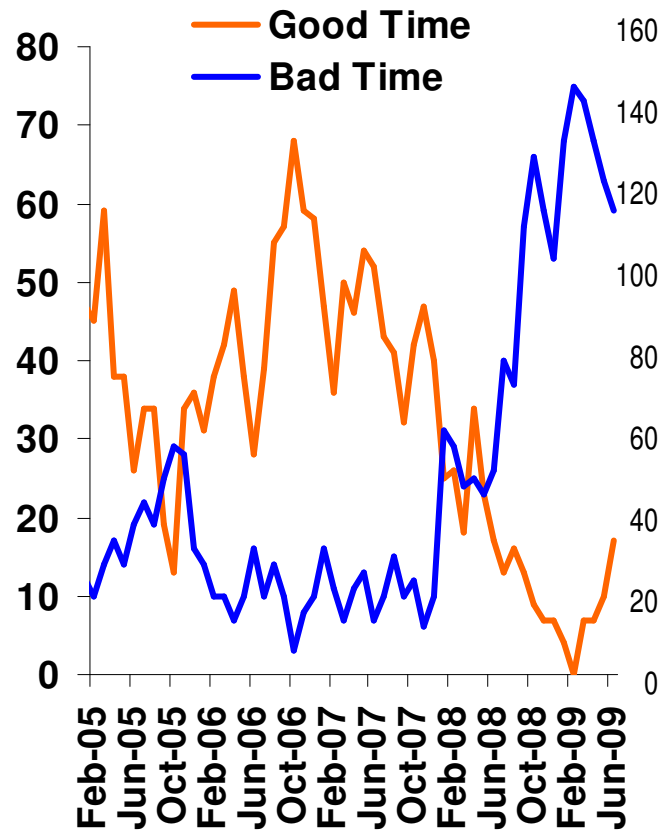
Producer confidence has improved significantly.

Confidence Indicator: Will the economic evolution be favorable in the next six months?
(percentage of answers)



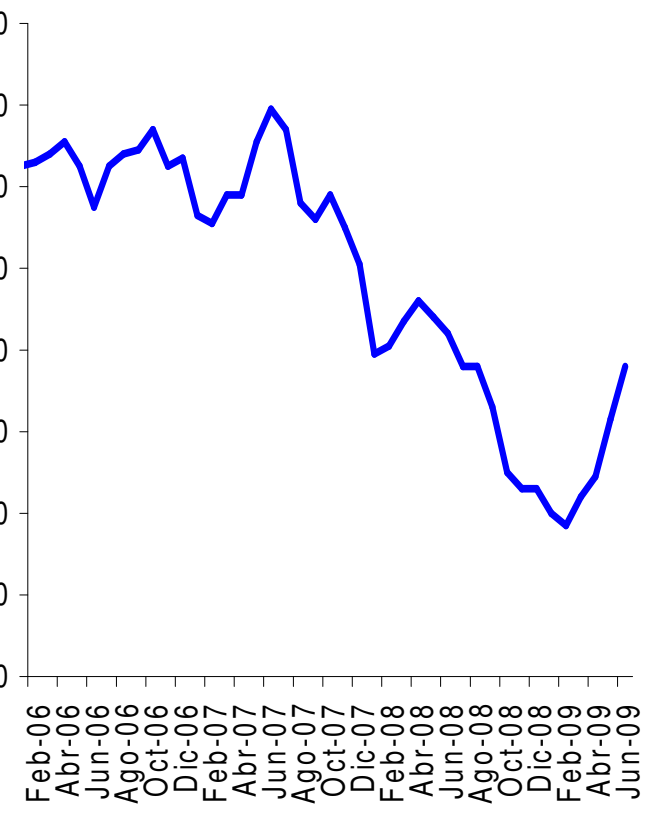
Source: Banco de Mexico

Confidence Indicator: Given the current economic situation, is it a good or bad time to invest?
(percentage of answers)



Source: Banco de Mexico

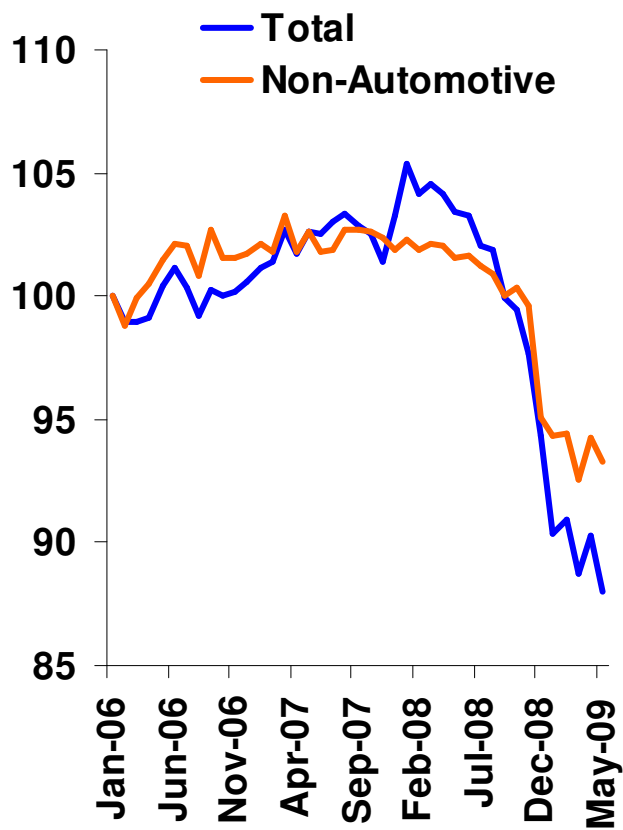
Confidence Index from Private Sector Analysts
(Index, 1998=100)



Source: Banco de Mexico

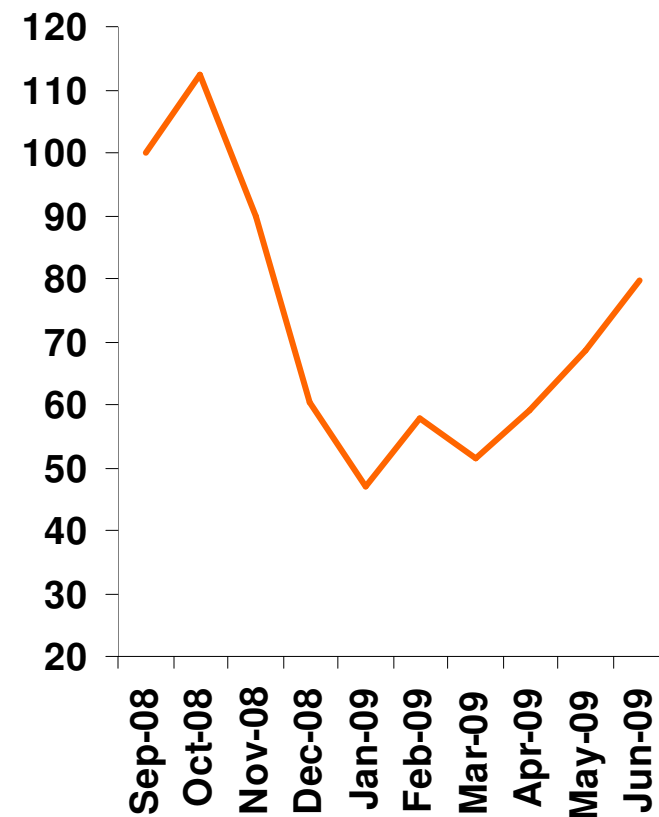
Manufacturing and automobile production was significantly affected by the problems in GM and Chrysler, given their high share of production in Mexico. Auto production of other firms has recovered significantly.

Manufacturing Production
(Index 2003=100)



Automobile Production (%)		
	2008	Jan-Jun-09
Chrysler & GM	37.5	28.7
Others	62.5	71.3

Automobile Production*
(Index, Sep-08=100)

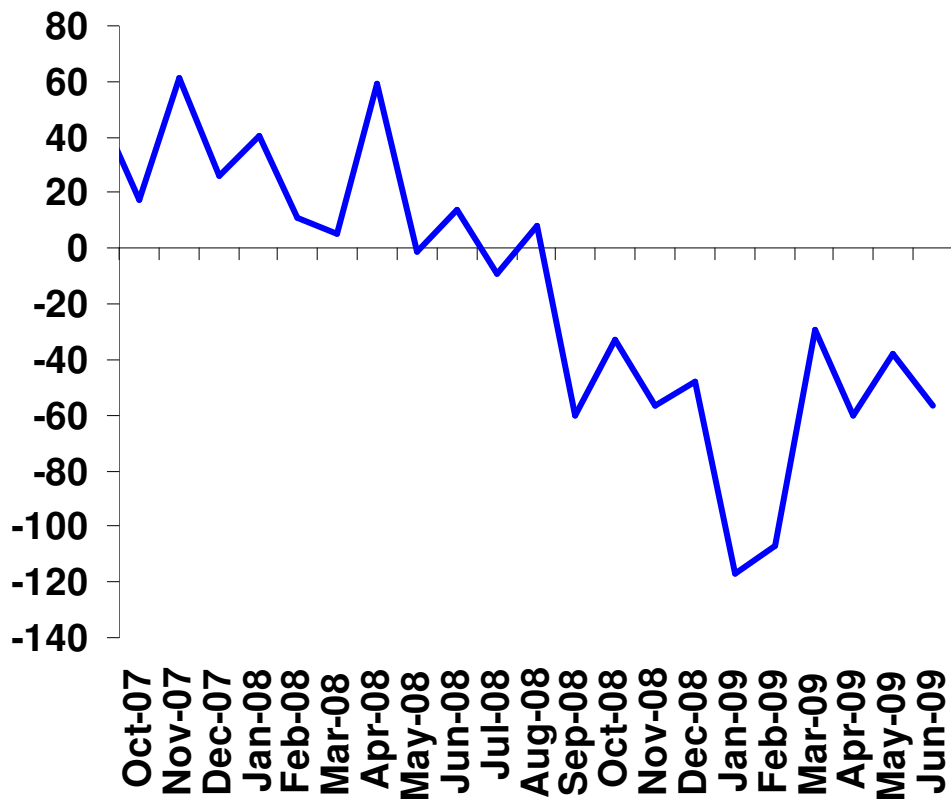


*Excluding GM and Chrysler.

Job losses moderated in March through June and the unemployment rate fell significantly in June.

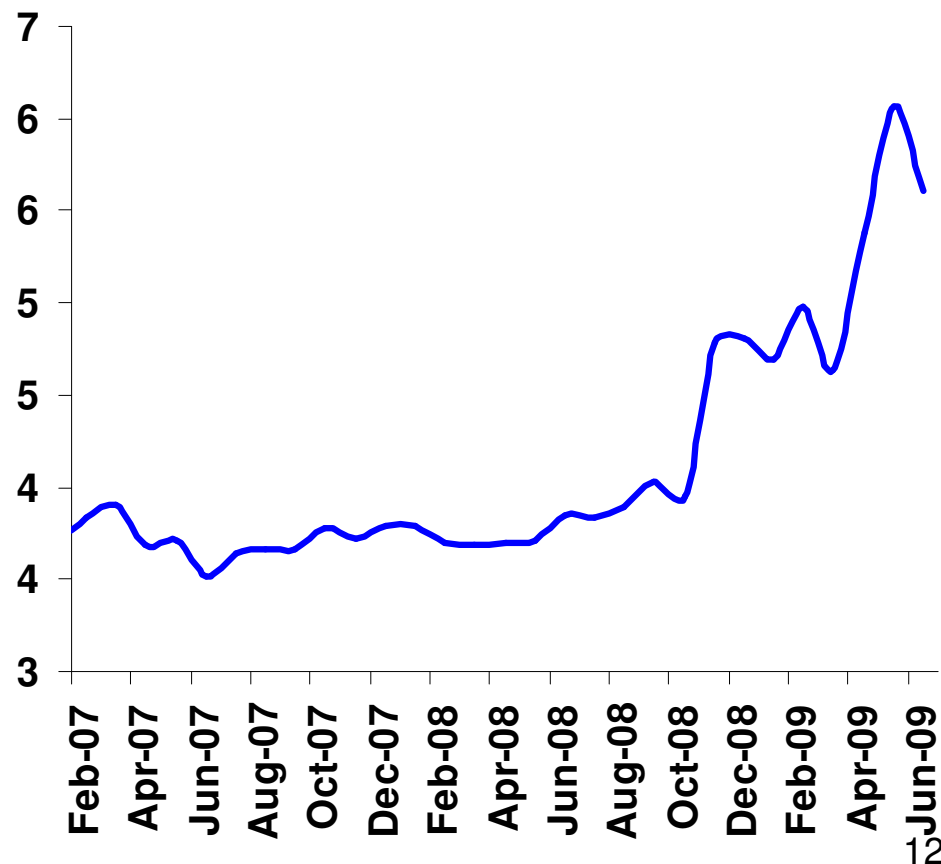
Employment, SA

(monthly change, thousand persons)



Unemployment Rate

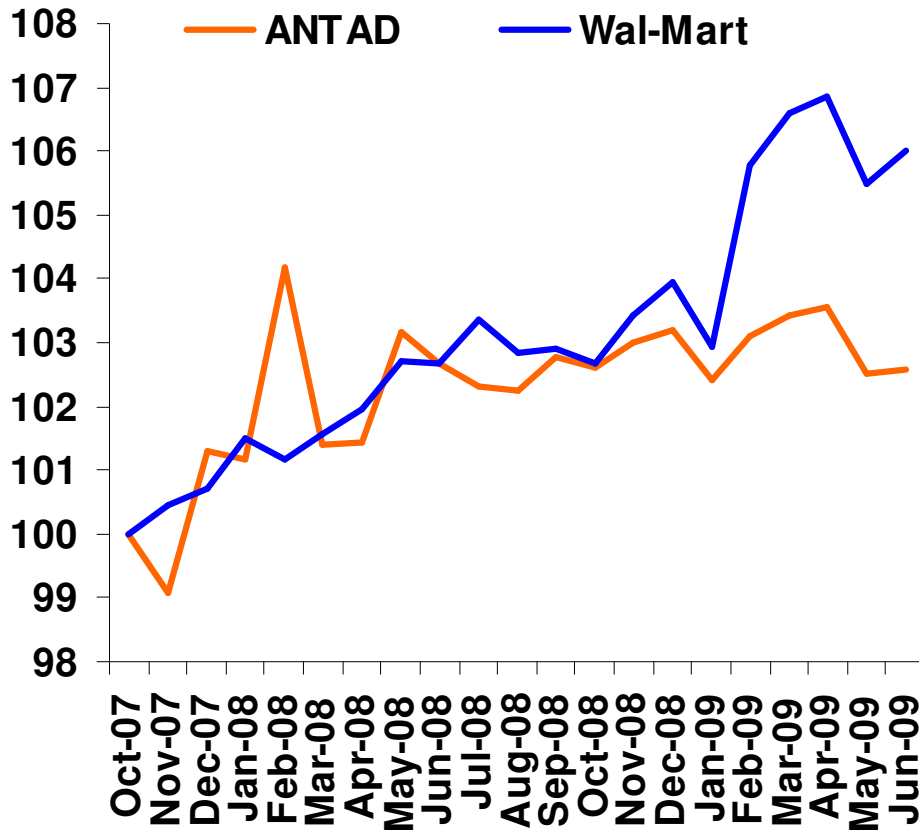
(%)





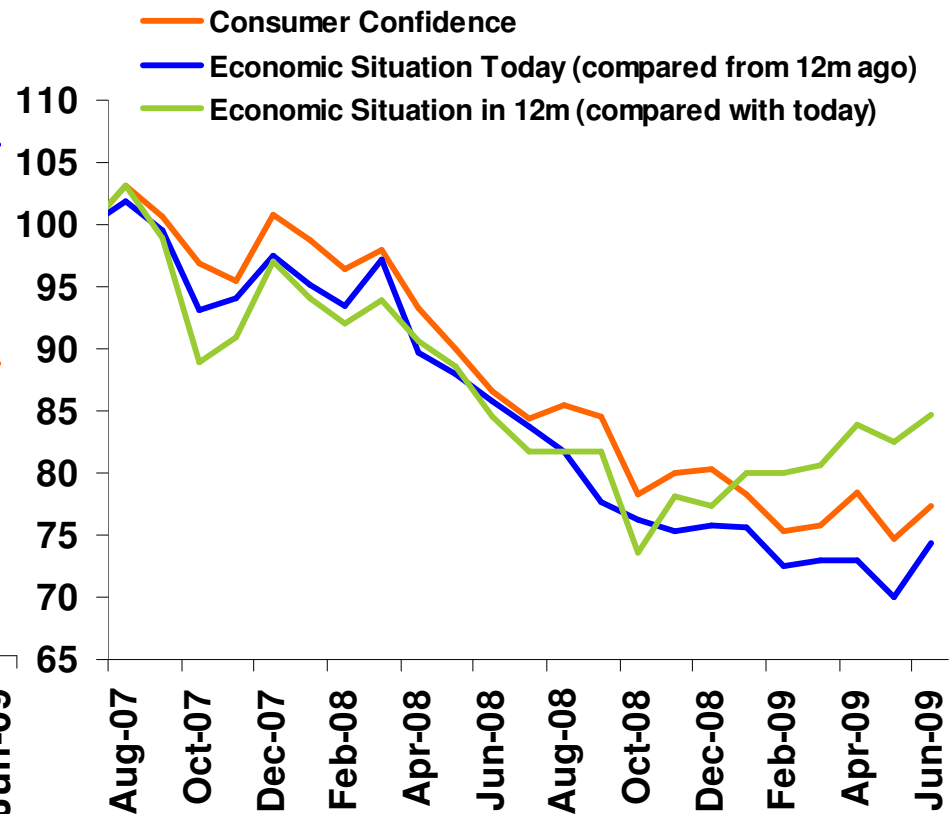
Although the recovery of final sales was temporarily interrupted by the flu epidemic, consumer confidence has stabilized and 12-month consumer expectations show moderate but sustained increases.

ANTAD and Wal-Mart Total Sales
(Index, Oct-07=100)



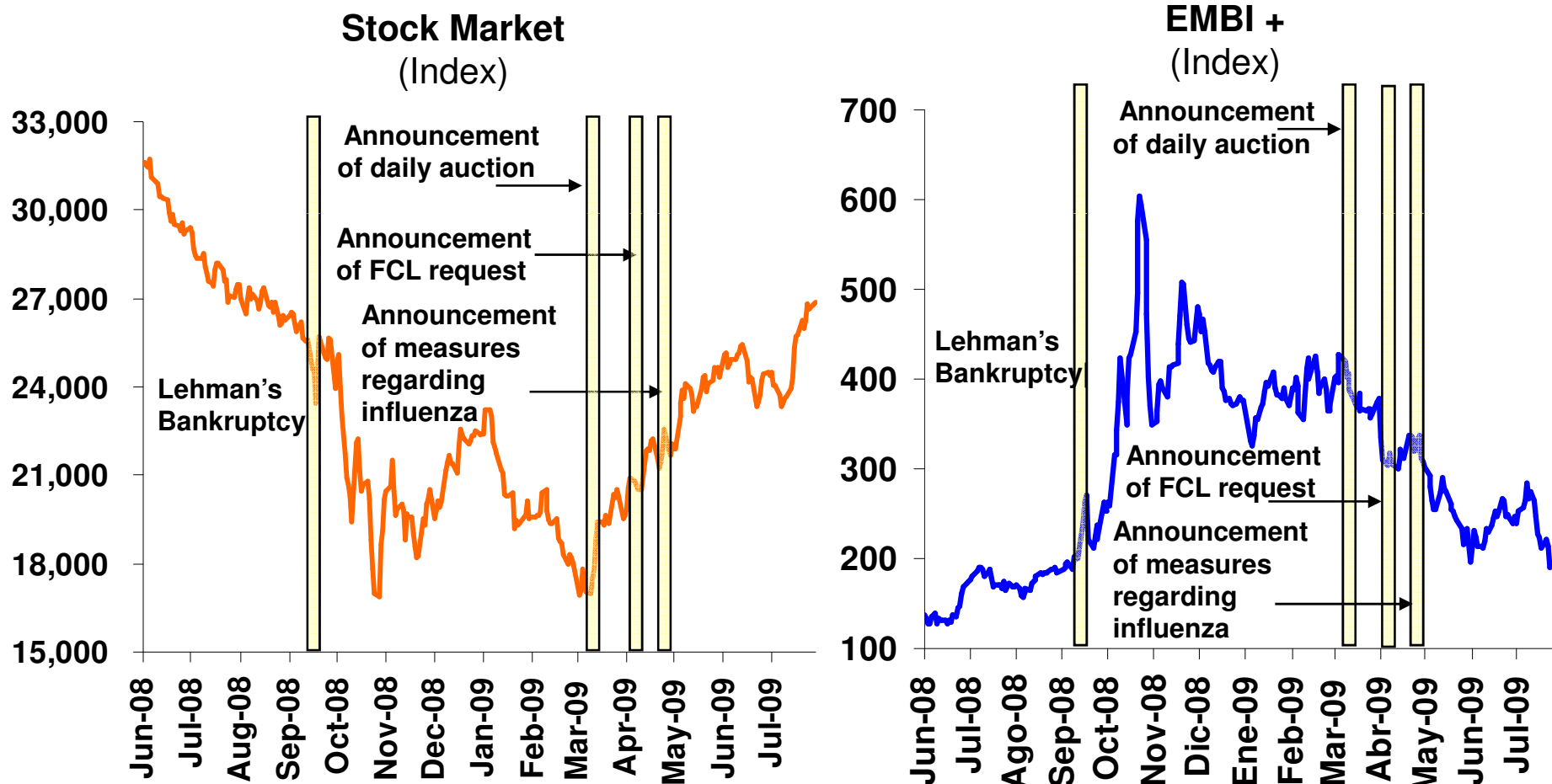
Source: Wal-Mart and ANTAD

Consumer Confidence
(Index, Jul-07=100)



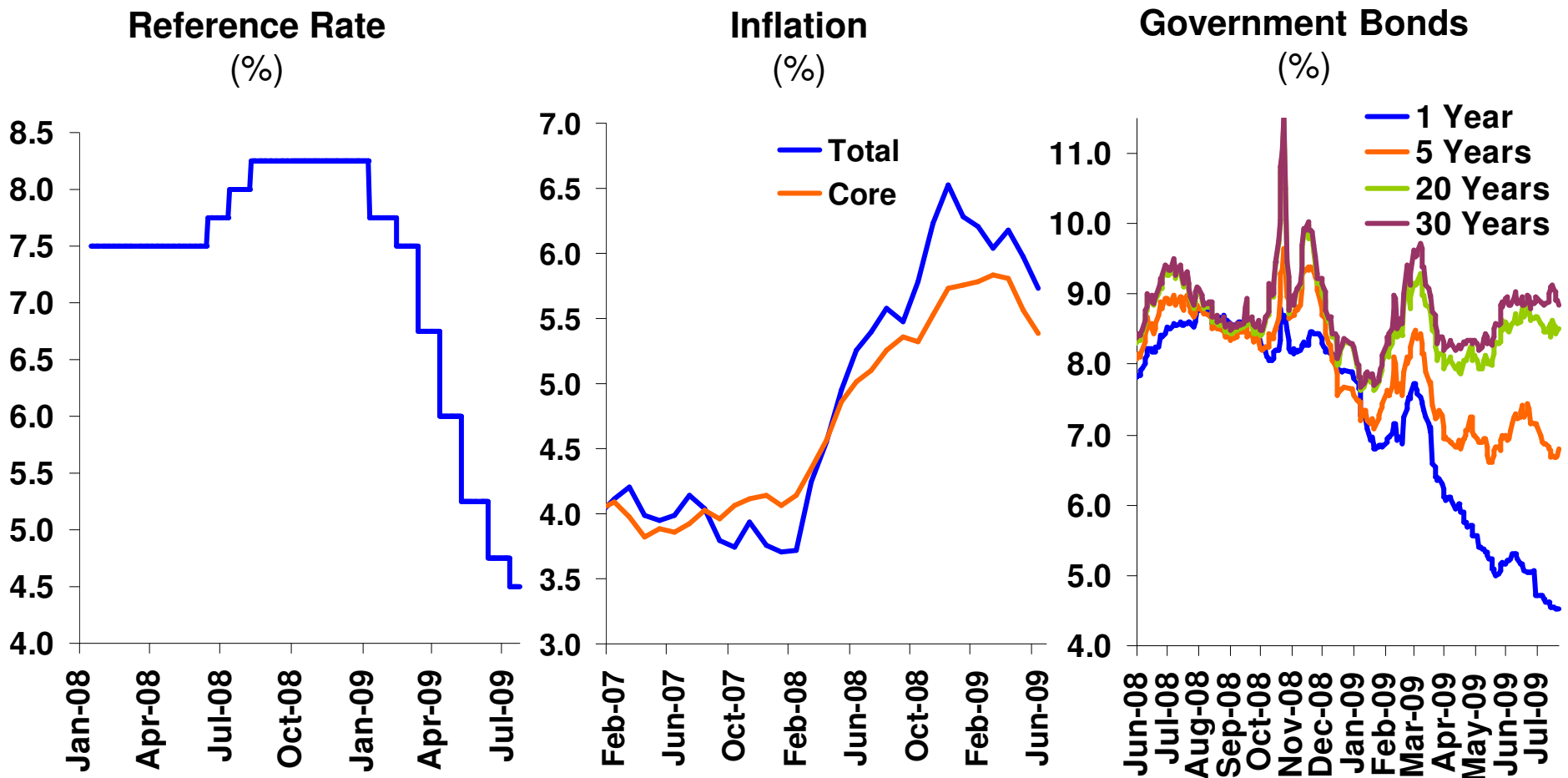
Source: INEGI

The stock market has recovered significantly in recent months, and country risk has fallen to levels observed before Lehman's bankruptcy.



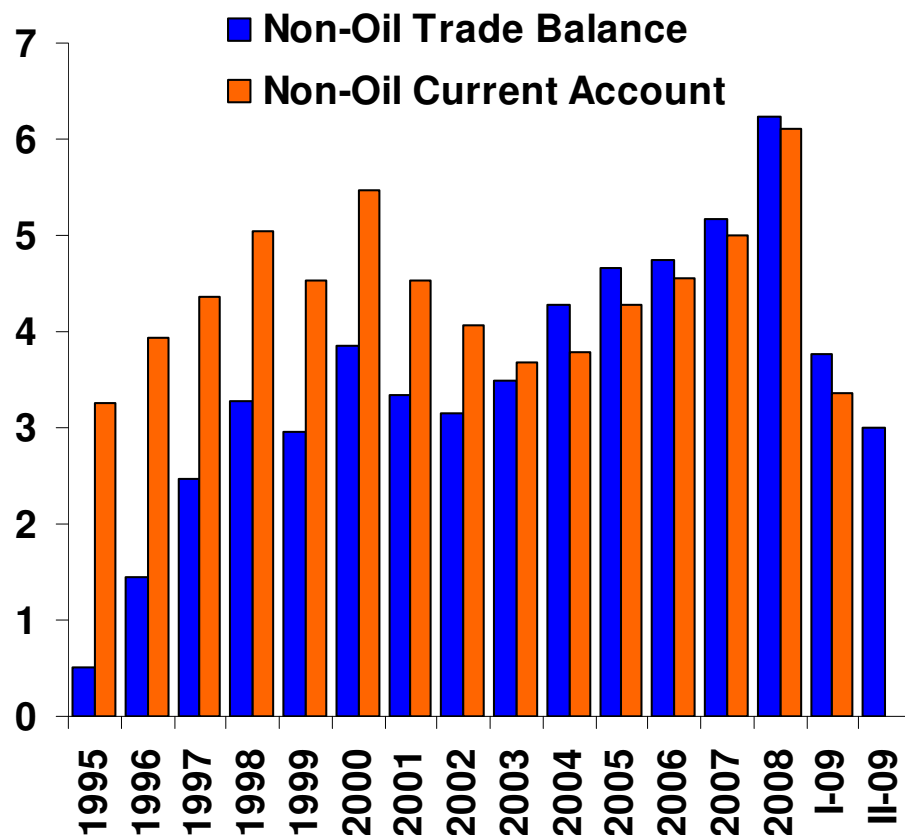
Source: BMV

Banco de Mexico has reduced its reference rate in response to lower inflation and economic activity. The increase in rates in the longer part of the curve is consistent with that observed in the U.S.



Mexico's non-oil current account deficit has decreased significantly and a moderate deficit is expected during 2009.

Non-oil Current Account Deficit and Trade Balance
(% of GDP)



Balance of Payments
(millions of dollars)

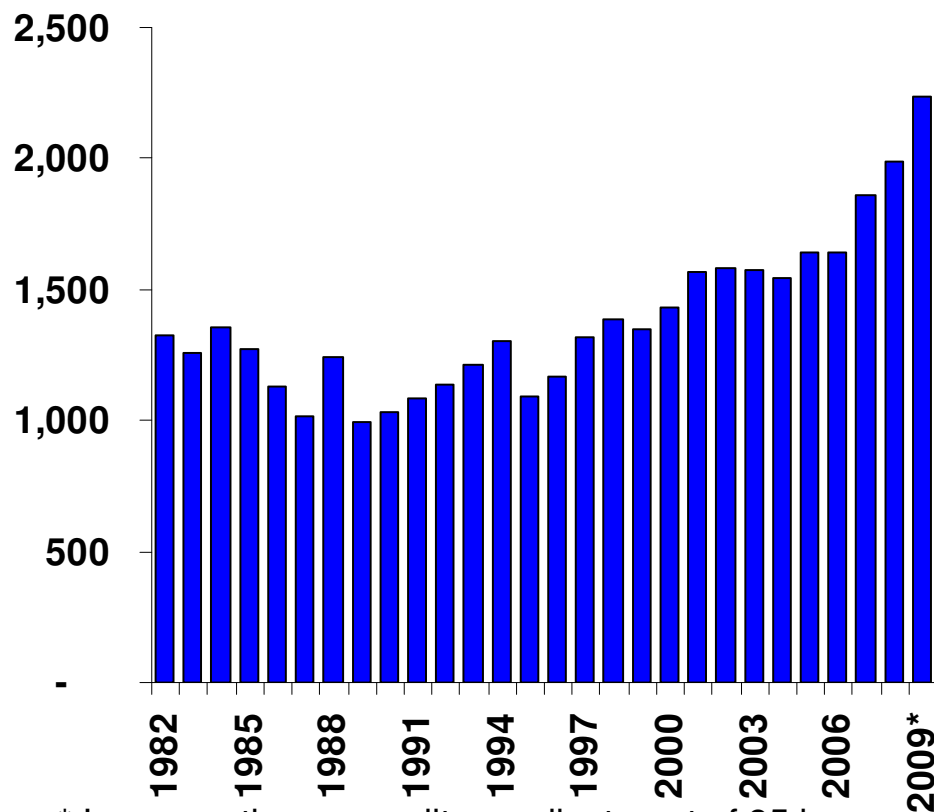
	2008	I-09	2009e
Current Account	-15,725	-1,067	-18,108
Trade Balance	-17,261	-1,890	-19,740
Oil-related Balance	14,381	5,463	8,170
Non-oil Balance	-31,642	-7,353	-27,910
Non-Factor Balance	-7,079	-696	-6,122
Factor Balance	-16,846	-4,019	-14,424
Balance of Transfers	25,461	5,539	22,178
Capital Account	24,550	-3,939	20,119
Liabilities	33,158	1,700	18,693
Indebtness	7,986	-34	7,013
Public	-3,928	955	10,613
Private	-939	-652	-3,600
PIDIREGAS	12853	0	0
Foreign Investment	25,172	1,734	11,680
Assets	-8,608	-5,639	1,426
Errors and Omissions	-1376	-1,591	-1,583
Variation of Reserves	7,450	-6585	428

A significant increase in the capital account is expected in the second half of 2009 due to the following:

- The revenues from the oil hedge.
- Disbursement of financing from the World Bank and IDB.
- Together with the fact that the daily sales of reserves have been reduced, this will lead to an increase in international reserves back to their level at end-2008 (USD 85 bn).
- In addition, the FCL by USD 47 bn. and the swap line with the FED by USD 30 bn. Implied there should be no problems to finance the BoP in the remainder of 2009 and in 2010.

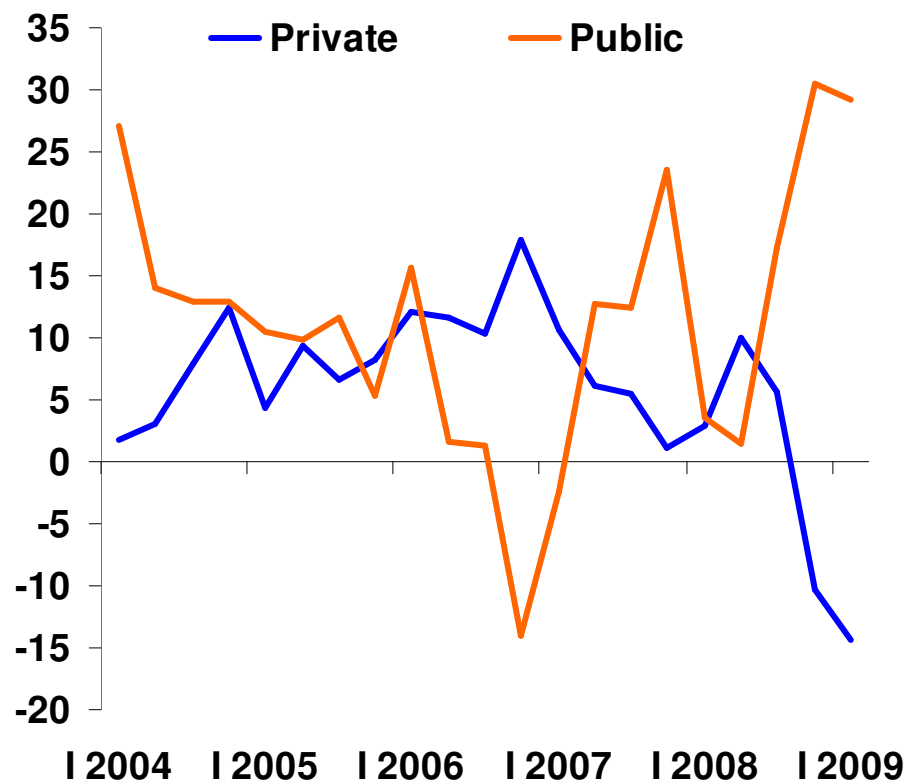
Even after the recently announced expenditure adjustments, fiscal policy is leading to an important boost to economic activity.

Approved Budget: Net Programmable Expenditure
(billion pesos of 2009)



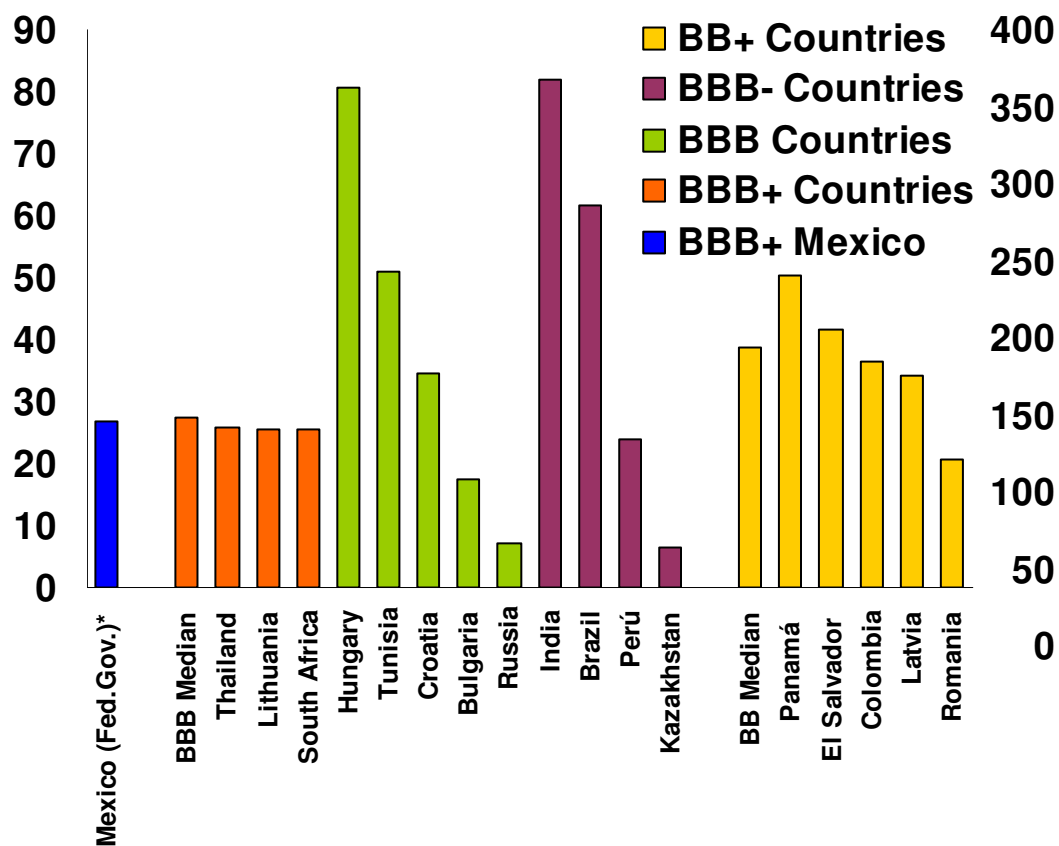
* Incorporating expenditure adjustment of 85 bn.

Investment
(annual change, %)

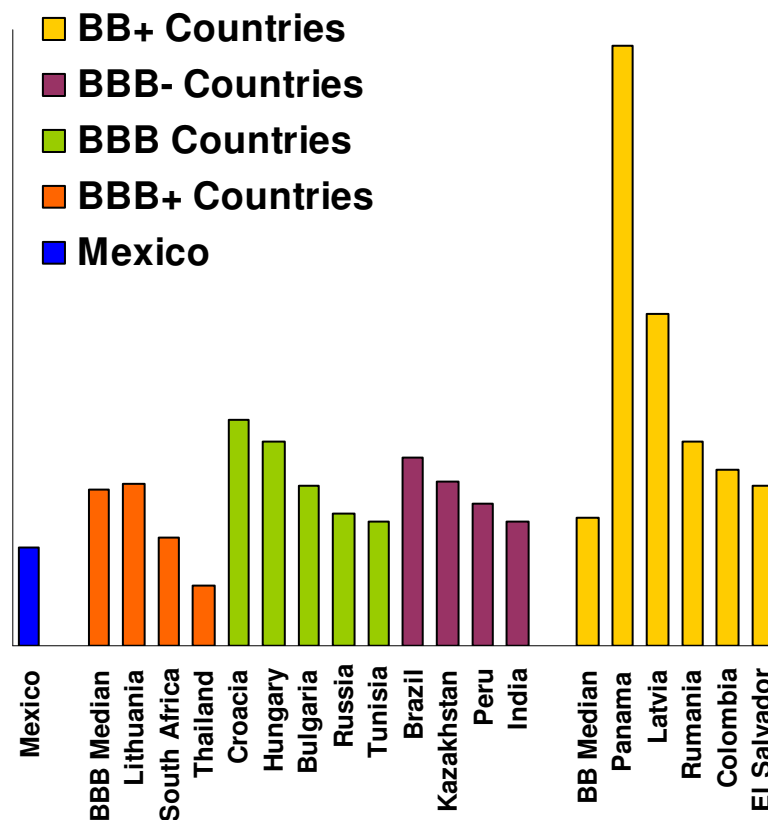


The countercyclical strategy has taken place in a context of fiscal prudence which has contributed to maintaining low levels of debt.

Federal Government Debt 2009 (% of GDP)

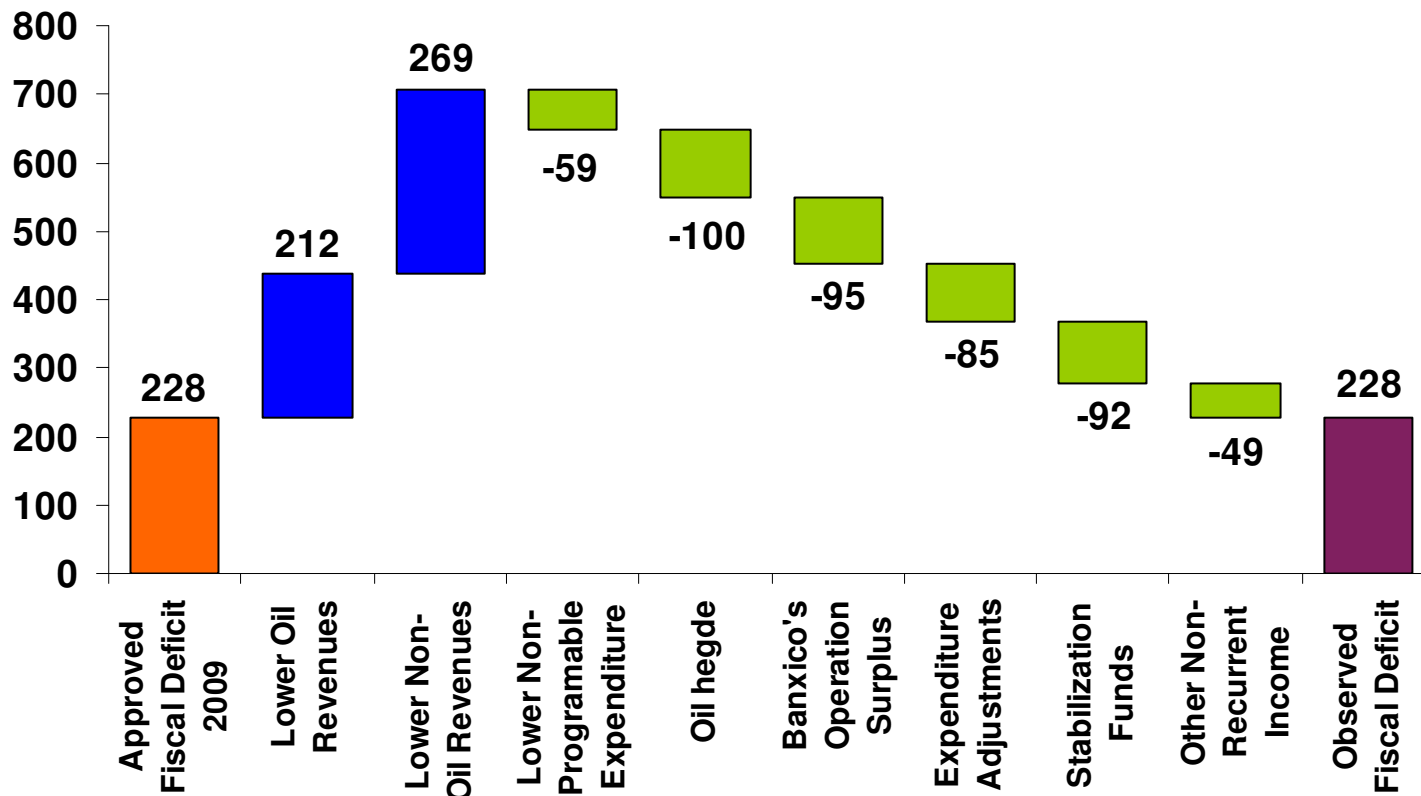


External Debt 2009 (% of current external receipts)



A shortfall in oil and non-oil revenues in 2009 will be compensated with resources from the oil stabilization funds, non-recurrent revenues and expenditure adjustments in order to maintain the same level of the deficit as was approved in the original budget for 2009.

Revenue Pressures and Funding Sources in 2009
(billion pesos, with respect to the budget approved for 2009)



Source: SHCP

Public Finances in 2010-2012 are facing two challenges:

- ① **A cyclical reduction in non-oil and oil revenues due to the global cycle:** The cyclical shortfall will be covered by having a transitory deficit or using non-recurrent revenues in the negative part of the cycle. The deficit will be smaller than the full cyclical reduction in revenues and will converge to zero in 2012 as the economy recovers.
- ② **A structural reduction due to lower oil production:** Falling oil revenues need to be gradually substituted with permanent non-oil sources of income. The fiscal measures that are required to close the structural medium term gap will also be used to moderate the deficit in the low part of the cycle.

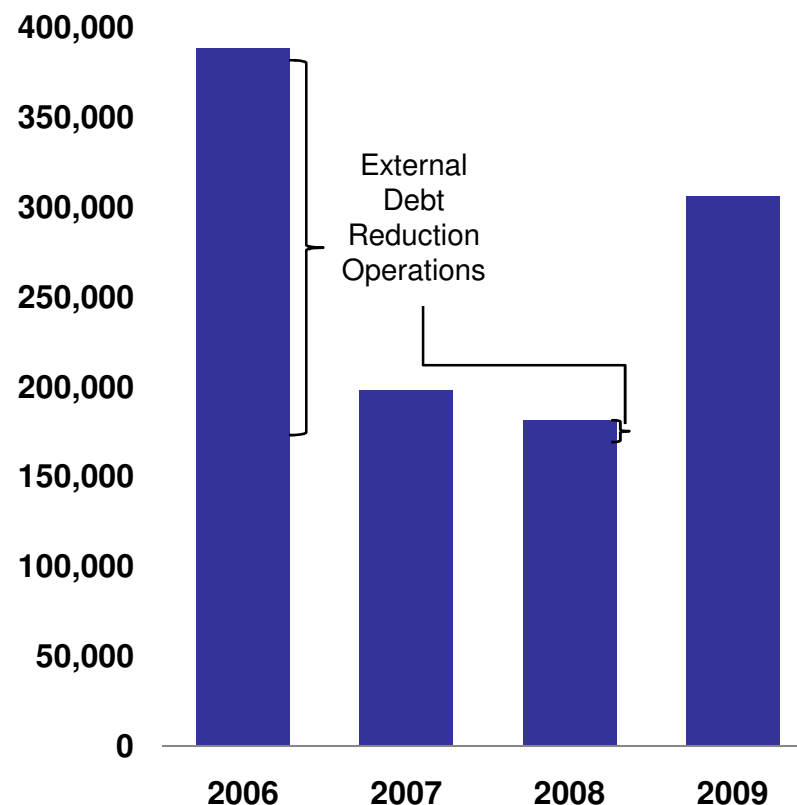
Therefore, the fiscal strategy will be based on four pillars:

- I. The adoption of a cyclically adjusted balance, with a moderate deficit in 2010 that will decrease in coming years as the economy recovers.
- II. The use of the resources in the stabilization funds and other non-recurrent revenues during 2010 and 2011, which will be used to make up for part of the cyclical shock.
- III. Measures to increase public sector revenues with an important effect in 2010 which will be increased in 2011 and 2012. This will make up for the permanent reduction in public sector income and also establish a higher permanent tax base.
- IV. Expenditure reductions.

In 2010, the increase in the Federal Government deficit should be financed without major difficulties and important flexibility through different sources.

- The increase of the financing needs is manageable in the context of the dynamics of the domestic market.
- The expected net multilateral financing for 2009 is around 5bn USD. This source can also be exploited in 2010.
- The access to the external markets will continue to be very important:
 - In the past months the issuance has been 3.5bn USD.
 - Access to other markets is being considered (Europe and Asia).

Financing in Domestic Market
(million pesos)



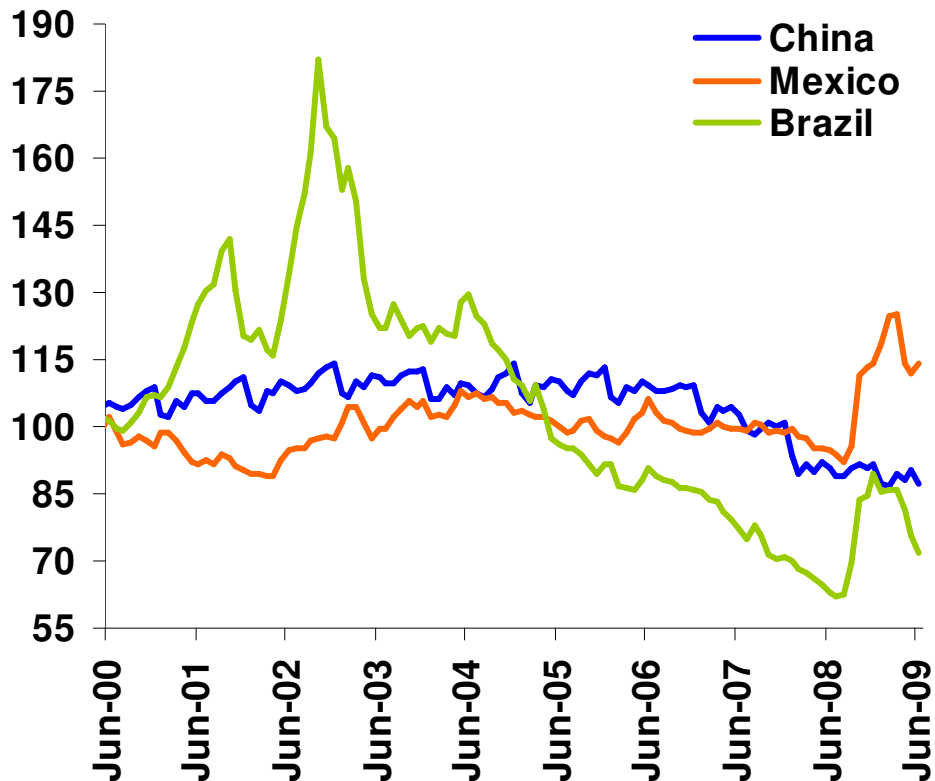
Source: SHCP

Going forward, the following elements will help sustain the recovery:

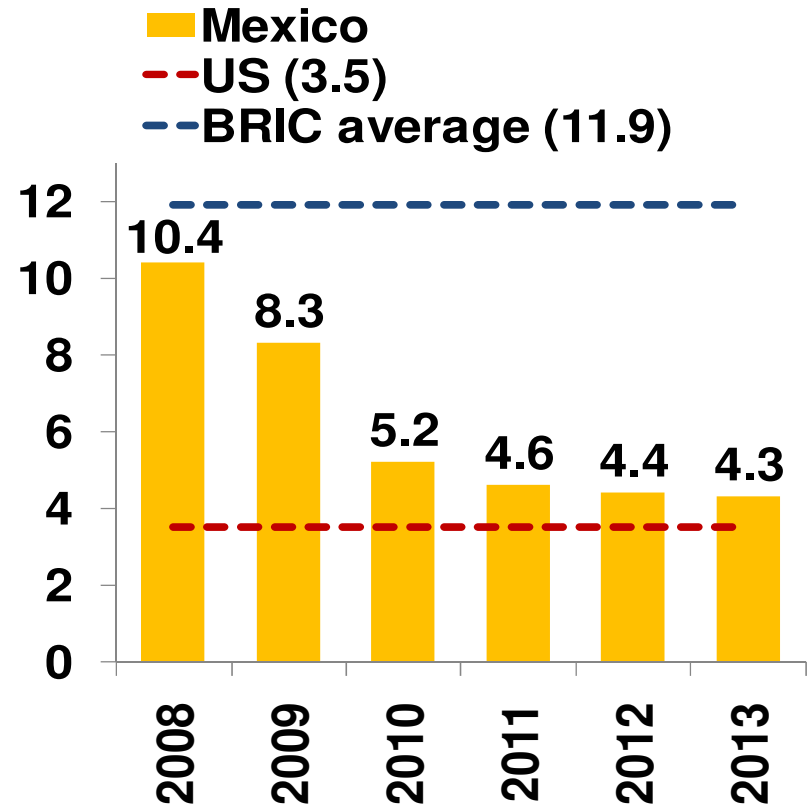
- Real exchange rate depreciation.
- High trade openness.
- Geography.
- Long term financing through the pension system.
- Energy Reform.
- Strong banking system.
- Investment in infrastructure.
- Development of the housing sector.
- Counter-cyclical policies.

A more competitive exchange rate should lead to a faster recovery in a context of higher trade openness.

Real Exchange Rate
(Index Jan-00=100)



Average Tariff on Imports
(%)



*US and BRIC average tariff on imports as of 2007.

The Energy Reform has several components that should lead to significant efficiency gains in PEMEX as well as a gradual recovery in production.

- Corporate Governance Reform.
- Performance-linked bonds.
- Greater flexibility in contracts.
- Budgetary reform for higher investment.

Large and Growing Source of Internal Savings

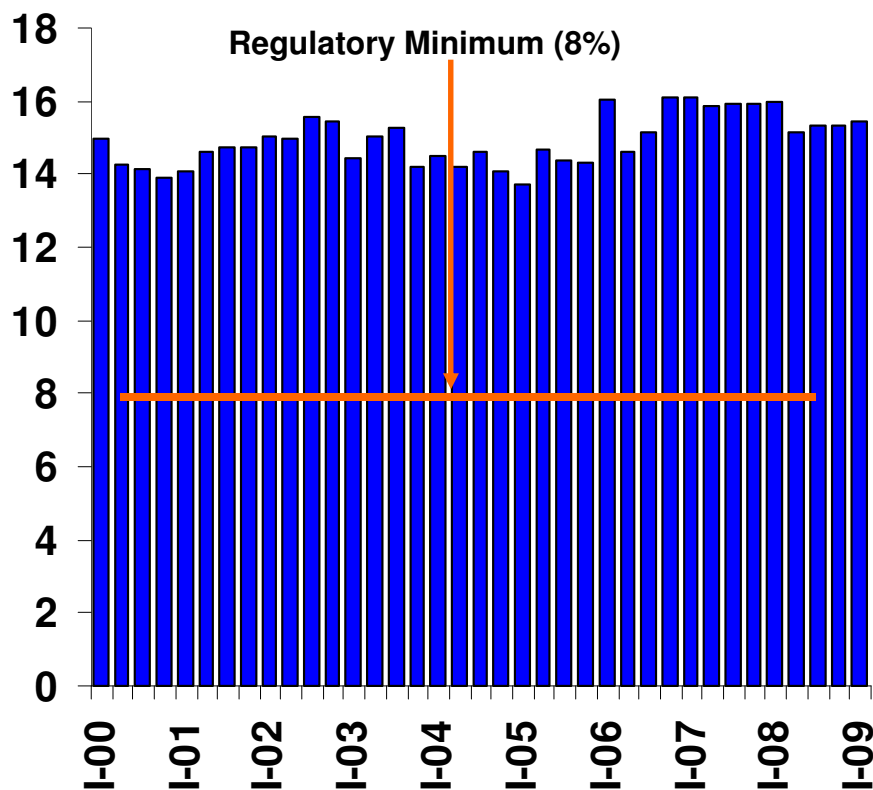


SHCP

High levels of capital and profits in commercial banks will allow for a strong recovery in credit once demand picks up.

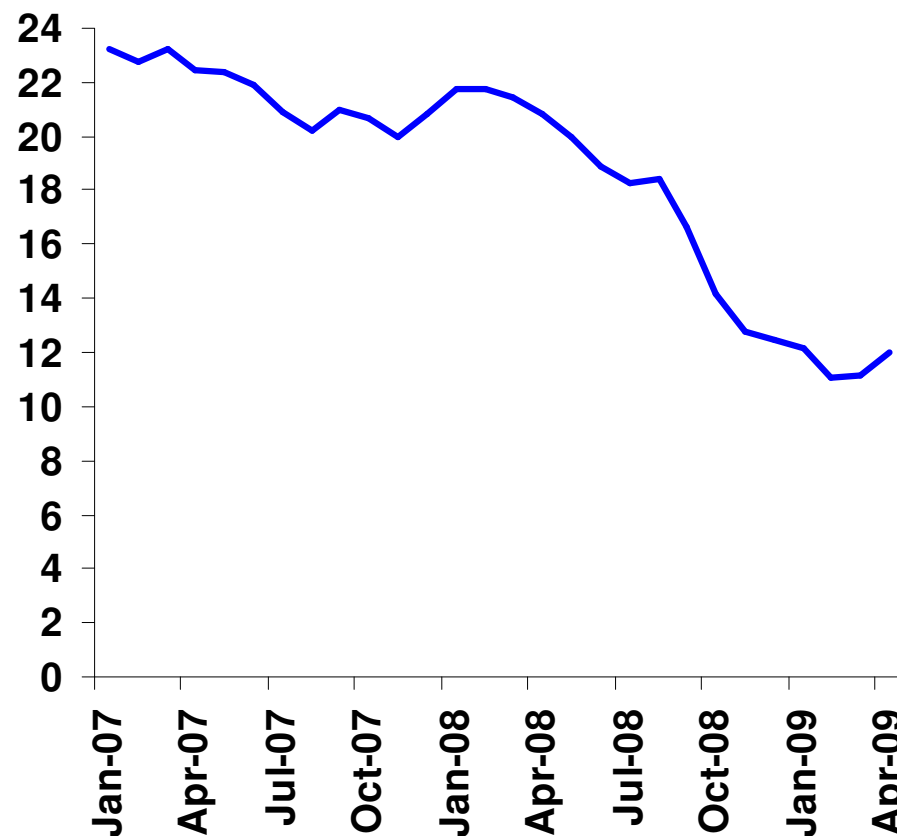
Capitalization Index

(net capital / risk weighted assets, %)



Return on Equity

(%)



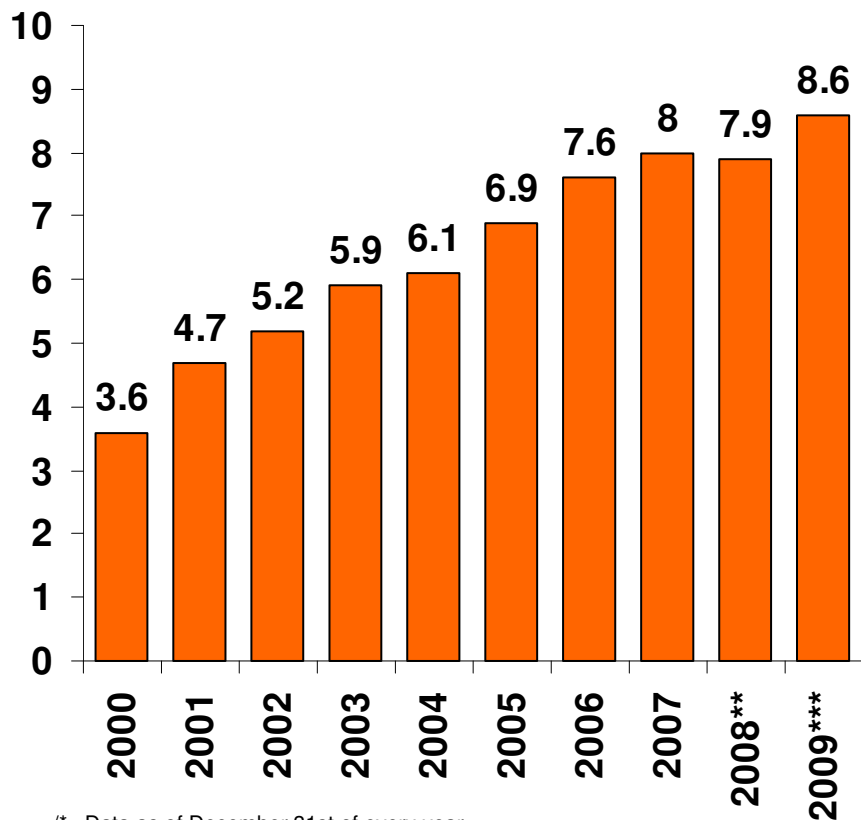
Large and Growing Source of Internal Savings



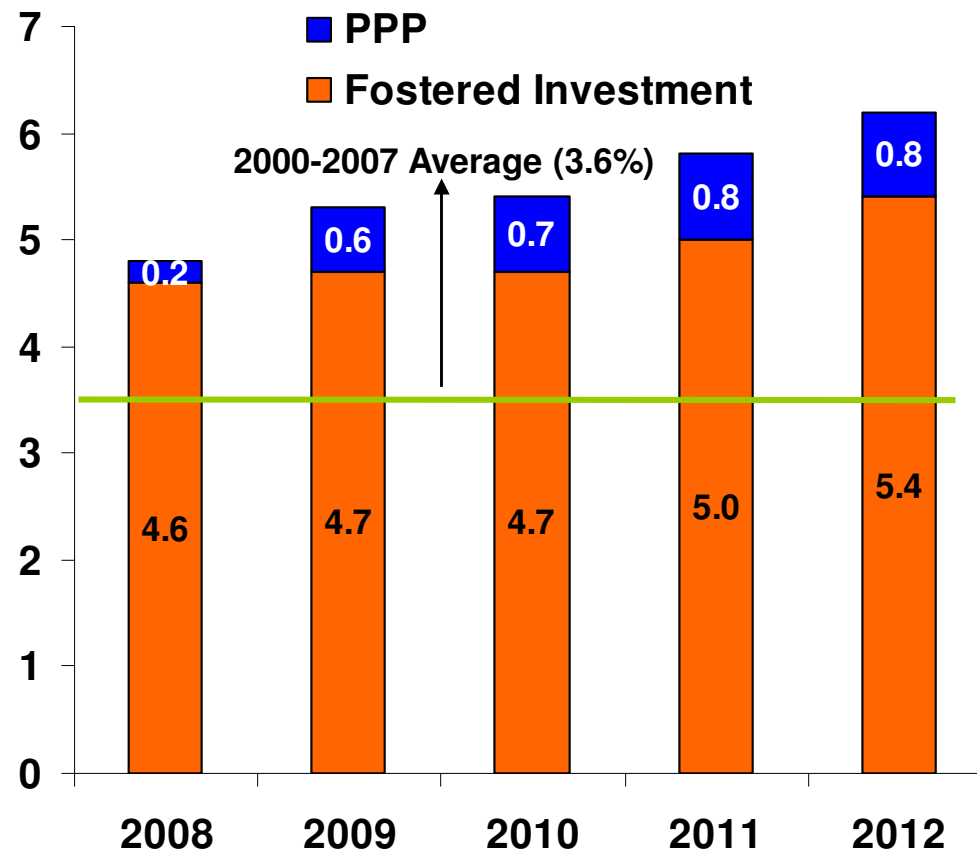
SHCP

The increase in the assets managed by pension funds should help to fund an aggressive program of infrastructure investment.

Assets Managed by Pensions Funds
(% of GDP)



Infrastructure Investment
(% of GDP)



/* Data as of December 31st of every year.
 /** Data as of January 2nd 2009.
 /*** Data for 2009 is estimated.

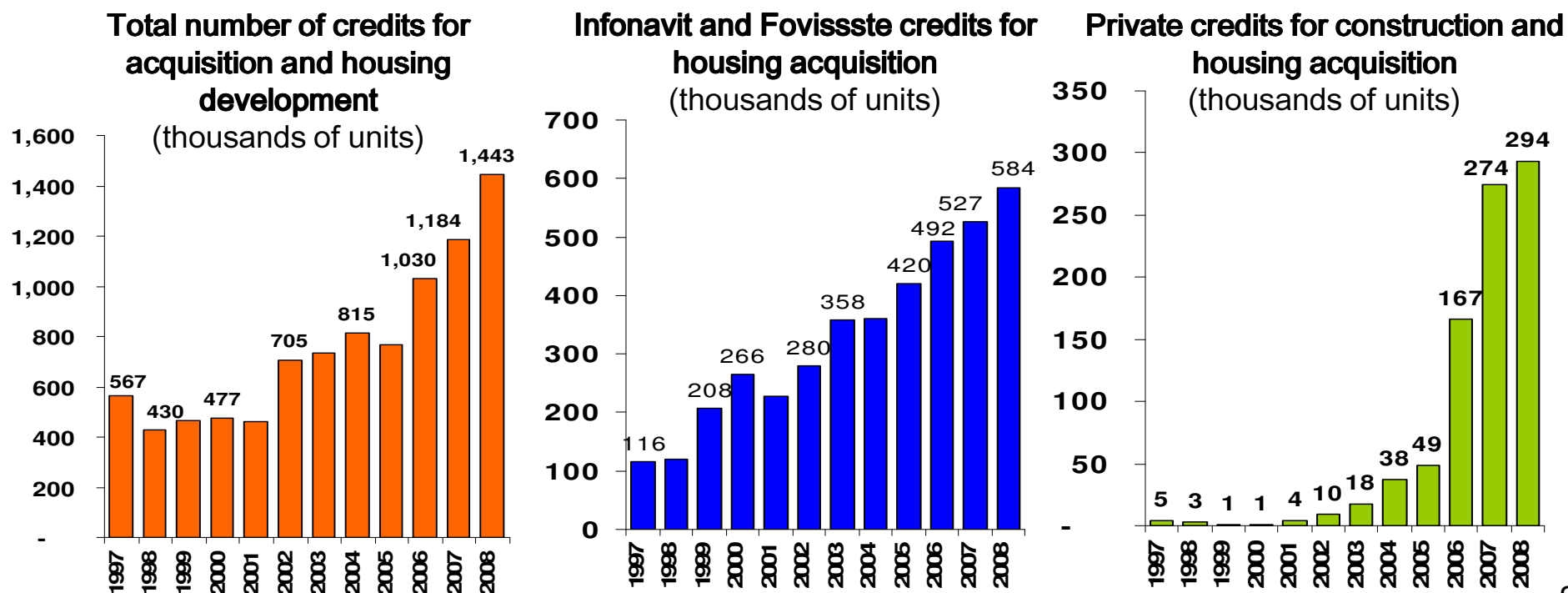
Housing Demand Supported by Public Financing



SHCP

The number of loans for acquisition and housing project development increased on average by 8.9% in real annual terms, going from 567 thousand to 1.4 million between 1997 and 2008.

- The public sector granted five times more credits for acquisition in that same period. Private sector credit for improvement and acquisition grew 46% on average per year.
- Credits for acquisition and construction reached their historical maximum in 2008 with 1,442,900 credits. INFONAVIT and FOVISSSTE granted 584 thousand credits in that year.



Final Remarks

- Even though initial signs of stabilization are being observed, and a recovery is anticipated during the second half of the year, this recovery will be gradual.
- Therefore, we need to continue with an ambitious agenda of reforms to accelerate growth and job creation.
- This should not only include measures to help in the fiscal adjustment, but also to promote greater competitiveness and competition in the Mexican economy.