

UNITED MEXICAN STATES
JANUARY 2009

CREDIT GUARANTEE COUNTRY PROFILE:

IES/02: ATTACHMENT N

Country Rating	S/T Business Cycle Indicator	S/T Political Indicator	Debt Recovery
2B	→/↓	→/↓	Debt recovery is best suited to the use of a good collection agent.

Credit Guarantee Experience

We remain open for cover on this market without any restriction, where we have a reasonable exposure and favourable underwriting experience. The market has, however, recently found themselves in a bit of a crisis due to the devaluation of the currency coupled with the ongoing global economic crisis. As such any exporters in this market on open account should ensure that they have taken the necessary measures to protect themselves against any non-payment that may arise.

Political Highlights

- ❑ President Felipe Jesus Calderon Hinokosa is expected to face a difficult environment in 2009 as the political focus shifting to the mid-term congressional elections in July 2009 will slow the pace of near-term momentum on his legislative agenda. A high level of violence stemming from organised crime represents a serious challenge to Mexico's deficient security forces.
- ❑ Mexico has increased its military expenditure over two thousand fold in the last ten years. Spending grew from \$145m in 1998 to \$10.7bn in 2008. President Felipe's administration granted \$95.2m within a year to the Armed Forces for anti-drug operations. Troops were increased from 189,000 in 1995 to the current 283,000.
- ❑ Mexico has issued a vehement rejection of the idea that it could be heading towards institutional collapse as drugs cartels undermine the Government's ability to maintain law and order. The Mexican foreign minister claims that the country is not a failed state following a report from the US stating that Pakistan and Mexico bear consideration for rapid and sudden collapse.
- ❑ A civil war is underway in Mexico. The president and powerful drug cartels are locked in a battle over control of the country. Tens of thousands of Mexican army are fully deployed and regularly fighting the Zetas (ex-Mexican army Special Forces trained in the US) who are now working for the cartels. Government has not been able to limit the on going violence and confrontations between the two warring factions throughout Mexico. To date some 7,000 Mexicans have died in this war. During 2008 Mexico's violent deaths broke historic records raising the death toll to 5,630 execution murders.

Recent Economic Highlights

- ❑ Fields covered in wildflowers instead of maize are signs that many citizens have left in search of better lifestyles in the US. In some small towns such as Chincua, remittances account for as much as 12% of the local economy. With the global slowdown however, remittances are becoming smaller. Between January-August 2008, remittances fell by 4.2% from the same period in 2007. Fears rose with the high October remittances as the central bank expected money coming into Mexico to be from those repatriating their savings after losing their jobs. Remittances from the US fell by \$2bn to \$23bn last year compared to a year earlier. Despite the fall, remittances remain the second most important source of income in the Mexican economy after oil exports.
- ❑ The opposition parties Partido de la Revolucion Institucional (PRI) and the Partido de la Revolucion Democratica (PRD) were alarmed by the national strike of fishermen amid the current economic crisis. Over 2000 boats of the Fishing Fleet are in ports of both national coasts, demanding a cut in fuel prices and increased attention to the sector by Government. Losses caused by the strike have exceeded 300bn pesos (\$22m) with about 350,000 direct and indirect jobs being affected. Combined with the 400,000 jobs lost last year as well as the price of seafood rising between 15% and 20%, the situation is turning critical.
- ❑ Economists, financial entities and analysts predict a negative outlook for the economy this year, stating that it will suffer a marked recession due to the financial crisis. They warned in late 2008 that GDP will be 0.08%, the worst economic growth rank since September 2001. They alerted that only 87,000 formal jobs will be created and salaries would fall in the first half of 2009.
- ❑ Morgan Stanley predicted that the economy will fall by 1.5% in 2009, the worst drop since 1983. The contraction involving thinning consumption and industrial slowdown, will cause absolute recession due to the strong ties between the Mexican and US economies.
- ❑ Mexico cut its benchmark rate for the first time in three years, shifting its focus from fighting inflation amid a global slide in interest rates. The central bank lowered the key overnight rate to 7.75% well above the 0% to 2% prevailing in the US, Europe and Japan.
- ❑ Inflation rose 6.5% in December 2008 due to high food and energy costs— its fastest pace since 2001. Growth dropped to 1.6% at the end of the third quarter – its lowest rate since 2003, as global downturn tightened credit and slashed demand for exports in the US – its top trading partner. President Felipe pledged 2bn pesos (\$150m) in spending to prevent layoffs, slashed household gas and electricity rates for some industries by as much as 20% and froze gasoline prices through the end of 2009. Inflation is forecast to slow to between 3.5% and 4.5% in 2009. The peso has lost about a third of its value

since October 2008. It weakened to near 14 to the dollar in December 2008. Government officials expect the economy to expand 1.8% this year, but a unit of Citigroup and one of Mexico's biggest banks predicts a 0.2% contraction.

- ❑ Revenue from the construction sector slid 30% last year as projects dried up amid the credit crunch. The president claims that infrastructure spending is too small and too slow to lift the economy out of recession this year. He promised to make spending on roads, bridges hospitals and sewage systems an engine for growth during his six-year term and increased government investment in such projects by 29% to 230bn pesos in the first nine months of 2008. There was a 0.2% drop in construction activity from January to October 2008. He pledged to boost investment from Government and private-sector partnerships by 7.5% in 2009.
- ❑ Mexico is planning a \$6bn resort on the Pacific to include 33,000 hotel rooms – an expanse twice that of Cancun. It is the largest tourist effort since Government helped build resorts in Cancun, Ixtapa and Los Cabos over two decades ago. The resort will accommodate 3m visitors a year by 2025 and bring in nearly \$3bn in revenue annually. Government will contribute over \$400m to complement \$5.5bn in planned private investment. Environmental activists have raised objections, saying that the development would damage an area of ecological richness. Overall tourism numbers reached 13m in 2008 – an increase of 5%.
- ❑ Mexican auto production and exports rose last year from 2007 but showed weakness toward the end of the year. Mexico produced 2.1m cars and vans last year, up 4% from 2007 levels. Exports were 3% higher than in 2007 at 1.7m units, while domestic new car sales fell 6.8% to 1m units. December's production was lower, exports fell 10% and domestic sales were down 20%. The auto industry, which has been affected by falling demand in the US market represents Mexico's largest single manufacturing sector.

Trade Developments

- ❑ Mexico will reduce tariffs on capital goods and other industrial imports to help support exporters hit by the recession in the US. Government will reduce tariffs on as many as 5,000 different classes of goods between 2009 and 2012. About 80% of Mexico's exports are to the US. The tariff reduction programme will be aimed at the automotive, manufacturing and export sectors, in particular the so-called maquiladora factories on the border that assemble goods for export to the US.
- ❑ South African exports to Mexico totaled R926m in 2005, R1.5bn in 2006, R1.3bn in 2007 and R179m in the year to March 2008, with imports totaling R2.1bn in 2007 from R1.9bn in 2006 and R576m in the year to March 2008.

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