December 2012
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Mexico: Arrangement Under the Flexible Credit Line and Cancellation of the Current Arrangement—Staff Report; Staff Supplement; and Press Release on the Executive Board Discussion

In the context of the arrangement under the Flexible Credit Line and cancellation of the current arrangement, the following documents have been released and are included in this package:

- The staff report on the arrangement for Mexico under the Flexible Credit Line and cancellation of the current arrangement, prepared by a staff team of the IMF, based on information available as of November 20, 2012. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.

- A staff supplement of November 21, 2012, on the assessment of the impact of the proposed Flexible Credit Line arrangement on the Fund's finances and liquidity position.

- A Press Release summarizing the views of the Executive Board as expressed during its November 30, 2012 discussion of the staff report that completed the request.

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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International Monetary Fund
Washington, D.C.

INTERNATIONAL MONETARY FUND

MEXICO

Arrangement Under the Flexible Credit Line and Cancellation of the Current Arrangement

Prepared by the Western Hemisphere Department
(In consultation with other departments)

Approved by Adrienne Cheasty and Lorenzo Giorgianni

November 20, 2012

Summary

- ***Background and outlook***. Mexico's growth has remained resilient, supported by both external and domestic demand, nearly closing the output gap opened during the global crisis. Mexico's strong economic performance, despite the sluggish U.S. recovery and persistent global uncertainty, attests to its strong fundamentals and sound policy management. Economic activity is expected to moderate towards potential growth next year. Inflationary pressures have been contained and expectations remain well-anchored, despite a recent uptick in headline inflation due to food prices. The exchange rate has fluctuated significantly, related to bouts of global risk aversion, but with no major balance sheet or pass-through effects. Policies have aimed to balance supporting the recovery and gradually rebuilding policy buffers. The incoming administration is firmly committed to maintain Mexico's strong policy frameworks and prudent macro policies.
- ***Risks***. Since the approval of the current FCL, global risks have remained high, particularly those that could trigger a surge in global risk aversion and generalized financial contagion.
- ***FCL***. In this context, the authorities are requesting a new two-year precautionary FCL arrangement, maintaining access at SDR 47.292 billion (1,304 percent of quota, from 1,500 percent originally approved in the current arrangement), and the cancelation of the current arrangement approved on January 10, 2011. They consider that, in a context where the external environment has become riskier, the FCL continues to play a critical role in support of their overall macroeconomic strategy and to provide a significant insurance against adverse global risks. The authorities considered the reduction in quota access as appropriate given the current risk balance. They underscored their intention to take further steps towards exit when improved external conditions allow. The staff's assessment is that Mexico meets the qualification criteria for access to FCL resources, and would recommend the approval of the arrangement on that basis.
- ***Fund liquidity***. The proposed commitment would have a manageable impact on the Fund's liquidity.
- ***Team***. This report was prepared by a team comprising Martin Kaufman (head), Herman Kamil, Esteban Vesperoni (all WHD); Pamela Madrid Angers (MCM); Santiago Acosta Ormaechea (FAD); and Gilda Fernandez (SPR).

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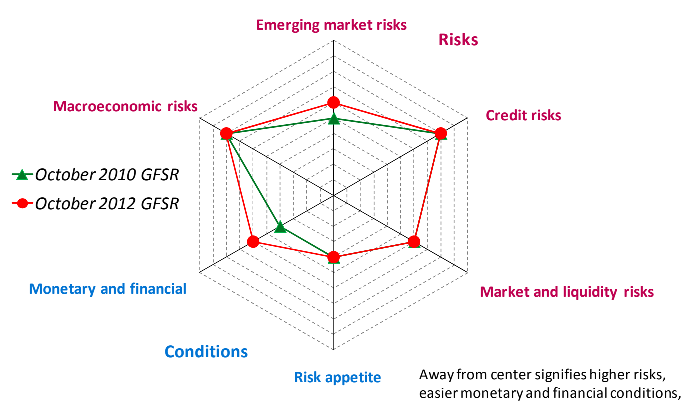
I. Context

1. **Mexico's strong economic performance attests to its strong fundamentals and sound policy management**. The strength and resilience of the recovery after the global crisis have been underpinned by Mexico's sound balance sheets, strong policy frameworks, and skillful macroeconomic management. The recognition of Mexico as a predictable and prudently managed economy, with market-friendly and transparent regulations for foreign investment, and open and liquid financial markets, have bolstered large foreign investment in recent years. Amid persistent global financial uncertainty, the successive FCL arrangements have supported Mexico's economic policies by providing a significant buffer against global downside risks. At the conclusion of the 2012 Article IV Consultation, Executive Directors commended the authorities for Mexico's strong rules-based policy framework and their skillful macroeconomic management.

2. **Despite Mexico's strong fundamentals, external risks continue to loom large in the context of its open capital account and large foreign portfolio investment.** Given its high integration with international capital markets, a surge in global risk aversion from an intensification of the crisis in Europe could affect even strong sovereigns like Mexico. The substantial equity and debt portfolio holdings of foreign investors (30 percent of GDP), including short-term government paper, mean that a generalized pullback from the emerging market asset class would be a material risk. The presence of two large Spanish bank subsidiaries also represents risks, which Mexico's subsidiary model and effective oversight help to contain. Moreover, a significant U.S. slowdown would be a major drag on growth in Mexico given its close integration with the U.S. economy, particularly the manufacturing sector.

3. **Since the approval of the current FCL, global conditions have remained highly unsettled, particularly with respect to potential downside risks that could trigger a surge in global risk aversion and generalized financial contagion.** Despite recent temporary respites in financial market turbulence, heightened risks to global financial stability persist, with a more adverse environment for emerging markets than in 2010. Key downside risks are associated with a re-intensification of the euro area crisis triggered by market reaction to insufficiently decisive policy action. Abrupt tightening of U.S. fiscal policy or uncertainty about raising the debt ceiling could also hurt markets and growth. Potential spillovers from the euro area crisis remains a significant concern for

Global Financial Stability Map



Source: IMF staff estimates.

Mexico, including from Spain's banking system given the presence of two large Spanish bank subsidiaries.[1]

II. Recent Developments

4. **Mexico's growth has been resilient, supported by both external and domestic demand**. Growth in 2011 and 2012 has remained above potential and is expected to help close the output gap that opened during the global crisis (Figure 1). Since the crisis, Mexico has benefited from both the relatively good performance of the U.S. manufacturing sector and a strong recovery in market share in the U.S. (due in part to improved relative unit labor costs). In turn, domestic demand has been supported by sustained growth in employment and in corporate and consumer lending.

- Inflationary pressures have remained contained, despite the recent uptick in headline inflation associated with food prices, while medium-term inflation expectations remain firmly anchored (Figure 2). Amid relatively slack labor market conditions (with lower migration to the U.S. implying higher labor market participation), wage pressures have remained subdued.
- Credit conditions have remained supportive of domestic demand. The banking system, including the domestic subsidiaries of Spanish banks, has been shielded so far from unsettled external conditions. Underpinned by strong capital and liquidity ratios, bank credit has expanded at a sustained pace. Market access conditions for corporates have remained favorable thus far, with spreads near historic lows.
- The exchange rate has fluctuated substantially, linked to the recurrent bouts of global risk aversion, but without major balance sheet or pass-through effects. Exchange rate flexibility has been a key shock absorber, while sovereign and financial markets have remained stable, including the banking sector. Capital inflows have continued, particularly into local-currency sovereign paper and across the whole yield curve. During periods of high global uncertainty, foreign investors have responded mainly by covering currency exposures (Figure 3), which has induced significant exchange rate volatility while maintaining stable interest rates on sovereign paper.

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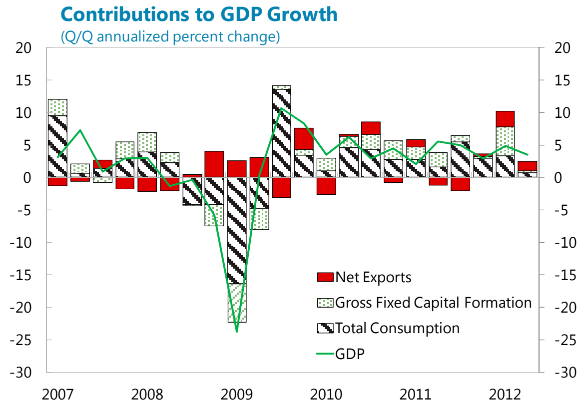
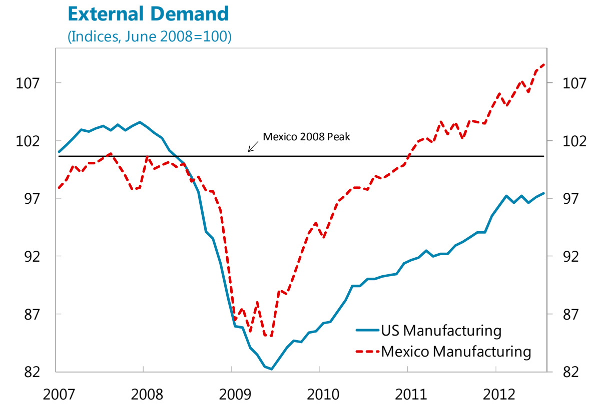
[1] The impact of the euro crisis may be amplified by its effects on U.S. growth, which is already projected at about 2 percent in 2012–13—against a projection close to 3 percent at the time of the approval of the current FCL.

Figure 1. Mexico: Real Sector, 2007–2012

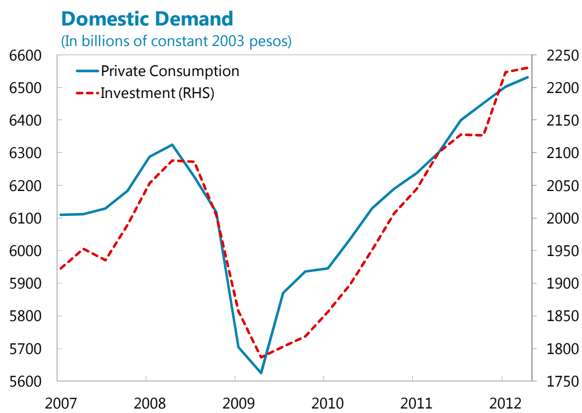
Growth has been resilient…



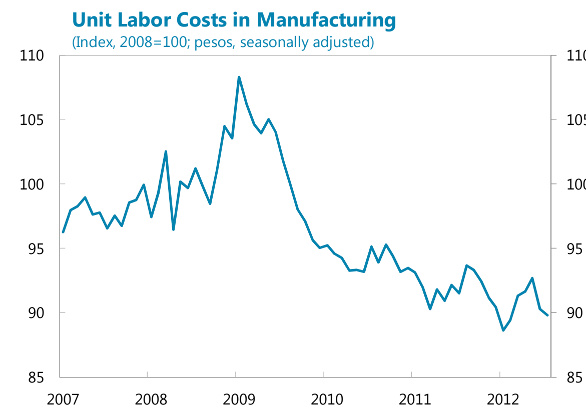
…supported by both external demand…



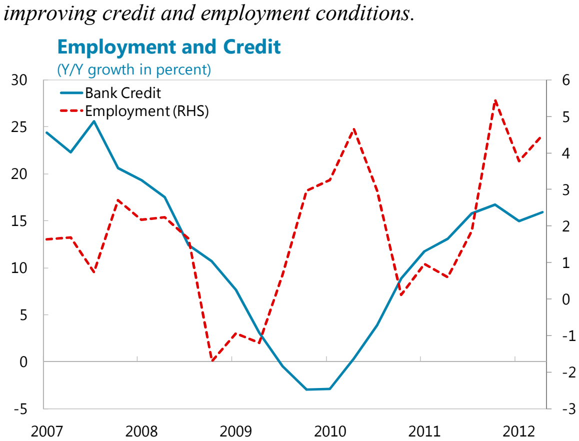
… and vibrant domestic demand.



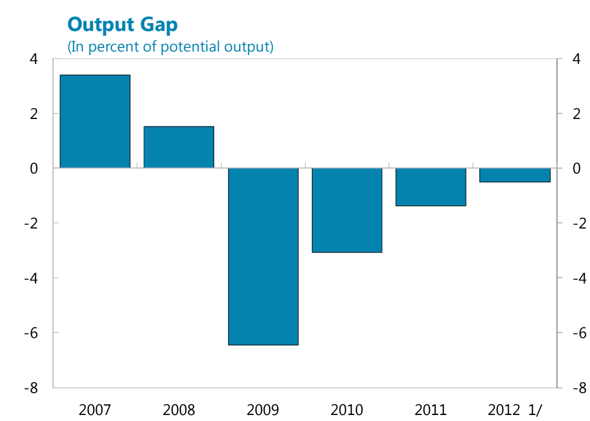
Exports have been underpinned by subdued ULC, amid lower migration to the US and higher labor participation…



… while buoyant domestic demand has been supported by improving credit and employment conditions.



Hence, the output gap has been gradually closing.

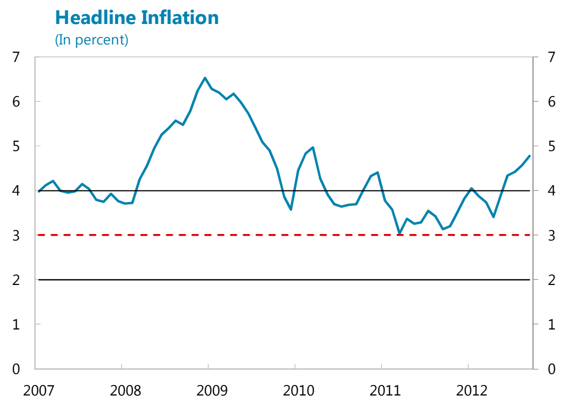


Sources: INEGI, Haver Analytics, Banxico, CNBV, and IMF staff calculations.

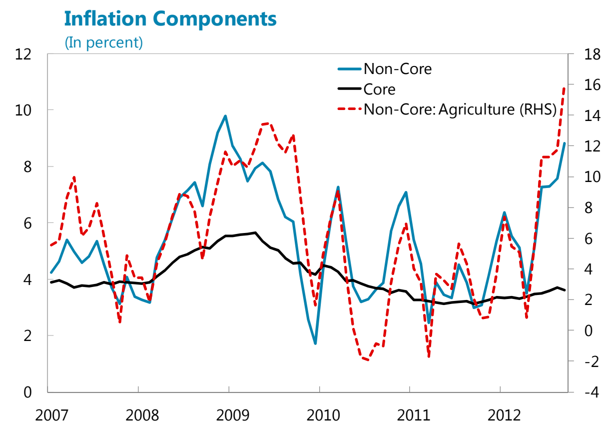
1/ Projection for 2012.

Figure 2. Mexico: Prices and Monetary Policy, 2007–2012

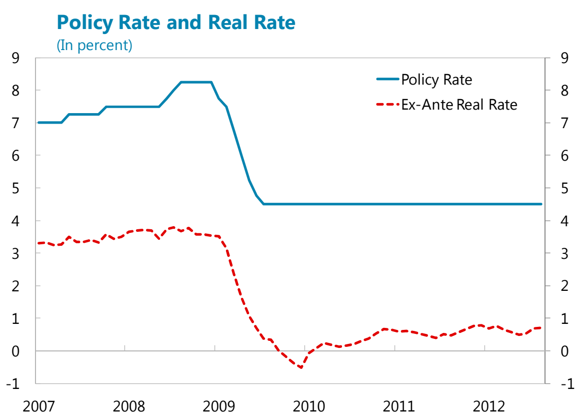
Headline inflation has moved above the target variability interval…



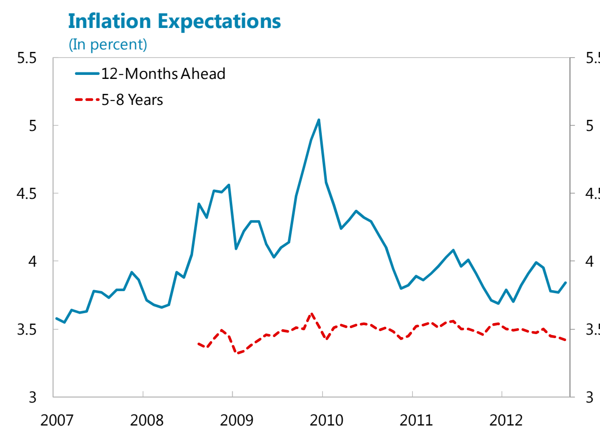
… driven primarily by agricultural prices, but core inflation has been broadly stable.



Monetary policy has remained stimulative…



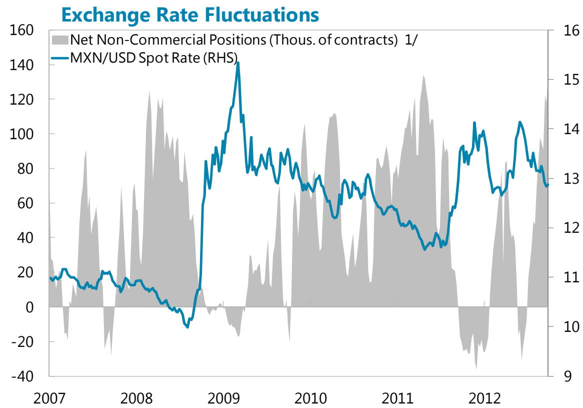
… amid well-anchored inflation expectations.



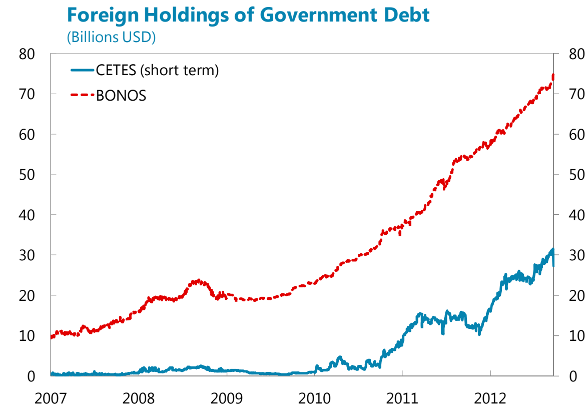
Sources: INEGI, Haver Analytics, Banxico, and Bloomberg.

Figure 3. Mexico: Financial Sector, 2007–2012

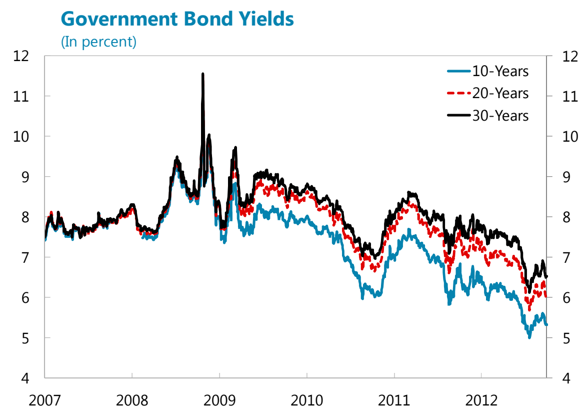
Exchange rate volatility has been associated with global uncertainty and hedging of peso positions…



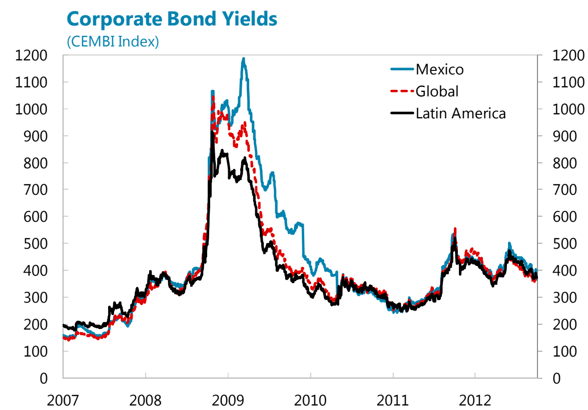
… while sovereign debt markets remained resilient.



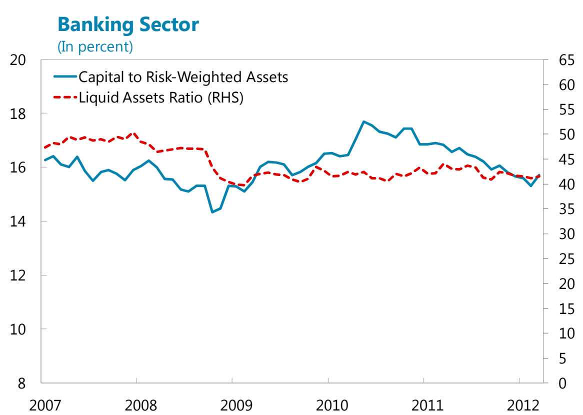
Sovereign bonds have recorded historically low yields…



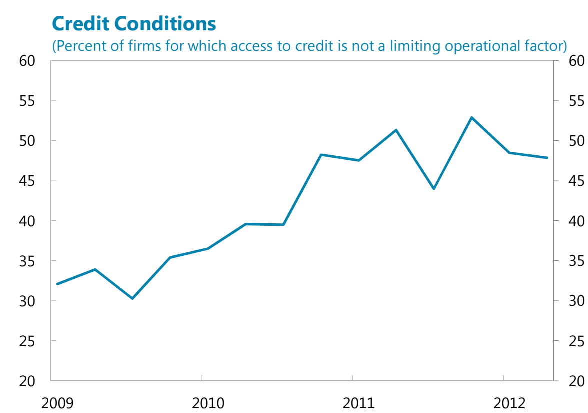
…while corporate yields are also subdued.



The banking sector remains liquid and well capitalized…



…while credit conditions have improved.



Sources: INEGI, Banxico, and Bloomberg.

1/ Non-commercial positions are those taken by traders that are not involved in the physical receipt/delivery of a commodity or asset.

5. **Mexico's external position has remained sound**. The Fund's current account models and a range of exchange rate metrics suggest that the external position and real exchange rate are consistent with underlying fundamentals and desirable policy settings. The balanced recovery in activity has meant that the current account deficit has remained moderate at about 1 percent of GDP (Figure 4). In the context of Mexico's rule-based reserve accumulation policy, the central bank bought US$16 billion in the first three quarters of 2012, with the bulk coming from Pemex's net FX balance; international reserves now amount to US$166 billion.[2] At the same time, capital inflows have increased the stock of foreign portfolio liabilities by US$48 billion in the first half of 2012, to US$355 billion (30 percent of GDP).

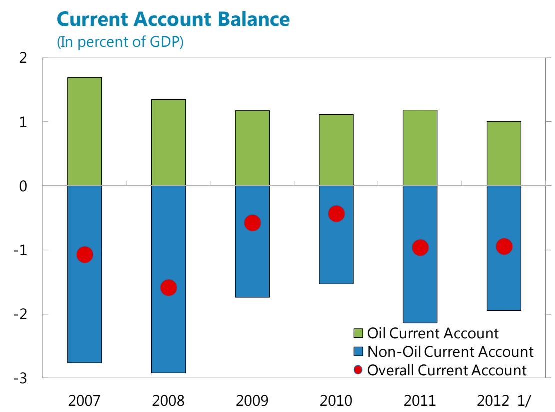
6. **Mexico's policy stance has judiciously balanced the need to support the recovery while gradually rebuilding policy buffers in the context of heightened global risks**. Mexico has continued to implement sound economic policies. Mexico's exchange rate flexibility has continued to play a key buffering role during the repeated bouts of global risk aversion. The central bank's rule-based intervention policy has sought to limit excess currency volatility.[3] Together with the flexible exchange rate regime, the policy mix—combining a gradual fiscal consolidation with stimulative monetary policy—has helped Mexico cope with capital inflows (Figure 5). The monetary authorities have maintained the policy rate at 4½ percent since 2009, and medium-term inflation expectations remain firmly anchored. Continuing with the fiscal consolidation, after the fiscal stimulus during the crisis, the primary deficit is expected to fall by about 1 percent of GDP in 2012 and return to balance. These consolidation efforts have helped stabilize public debt at around 43 percent of GDP.

[2] The rule-based reserve accumulation policy establishes that the proceeds from Pemex's net FX balance and the central government foreign currency net debt placements have to be sold to the central bank.

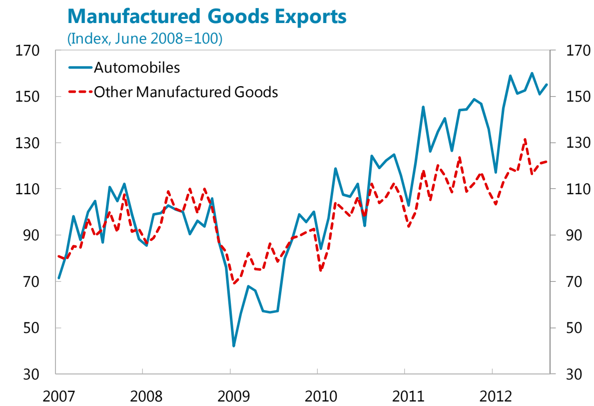
[3] The new rule stipulates that the Central Bank stands ready to sell up to US$400 million on any day that the peso depreciates by more than 2 percent from the previous closing.

Figure 4. Mexico: External Sector, 2007–2012

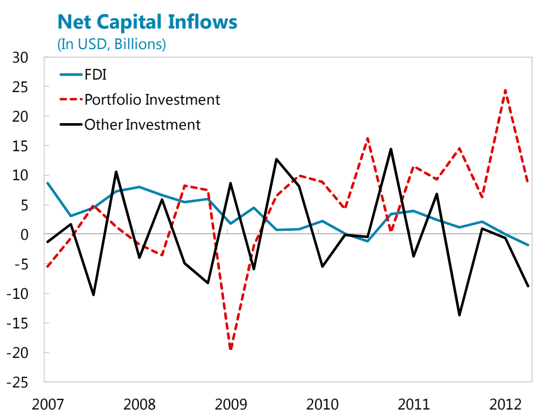
The current account has remained in moderate deficit…



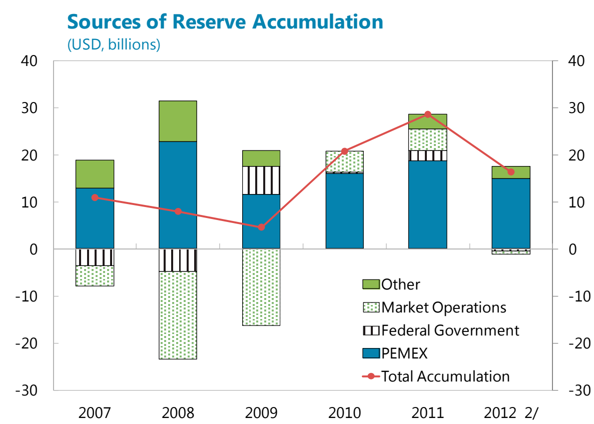
…with strong performance of manufacturing exports.



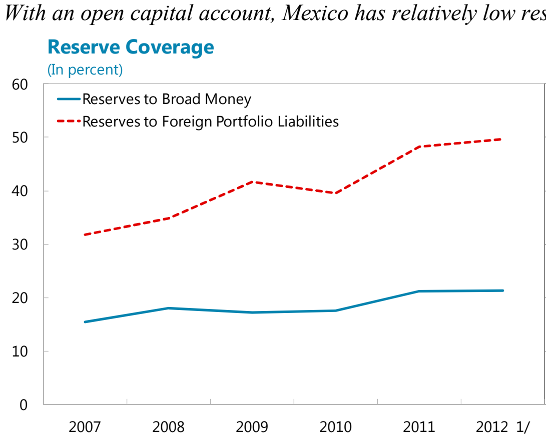
Foreign portfolio investment has remained strong…

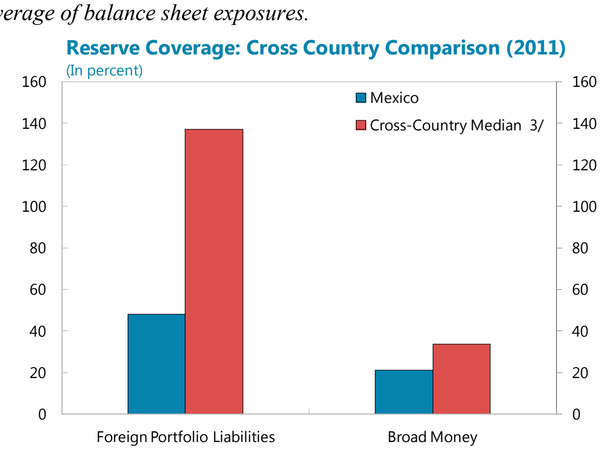


…and reserve accumulation has maintained a steady pace due to robust oil revenue…



With an open capital account, Mexico has relatively low reserve coverage of balance sheet exposures.

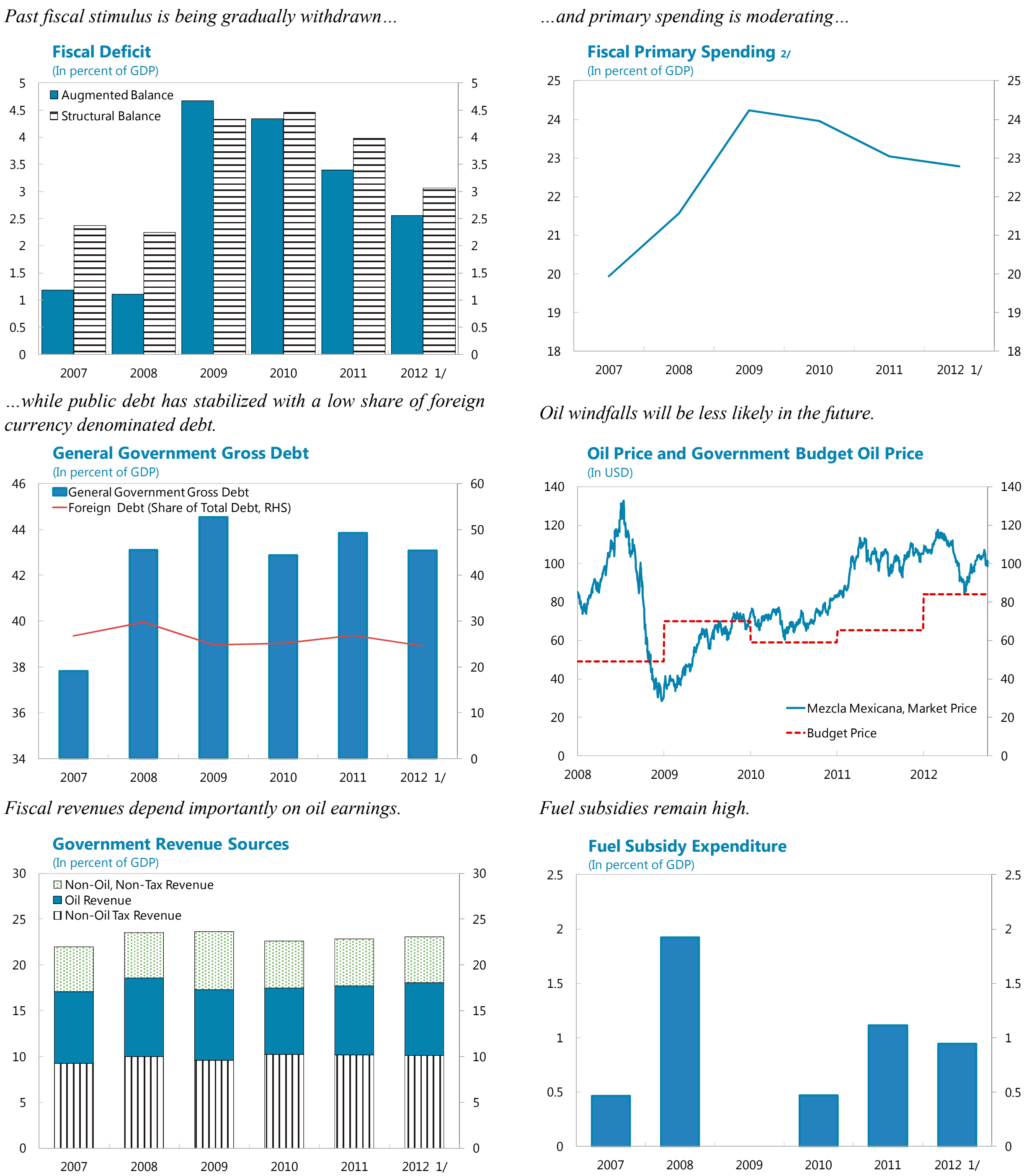




Sources: INEGI, Haver Analytics, Banxico, and IMF Staff Calculations

1/ Data based on IMF staff estimates.
2/ 2012 data based on data available through September 2012.
3/ Group of countries listed in Figure 8 and Figure 9.

Figure 5. Mexico: Fiscal Sector, 2007–2012



Sources: INEGI, Banxico, Bloomberg, SHCP, and IMF Staff Calculations

1/ 2012 data based on IMF staff calculations.
2/ Fiscal primary spending includes budgetary adjustments.

III. OUTLOOK AND NEAR-TERM POLICIES

7. **Growth is expected to moderate towards Mexico's potential rate in 2013**. Growth next year is envisaged to converge to 3½ percent, close to Mexico's long-term potential growth rate. External demand is expected to contribute moderately while domestic demand is envisaged to maintain its momentum, underpinned by sustained business and consumer confidence. High capacity utilization rates are expected to continue to underpin the recovery in fixed investment, while favorable credit conditions and sustained employment growth should help to support consumption. As food price shocks dissipate, headline inflation is expected to revert towards the inflation target.

8. **With the new administration taking office in December, policy continuity is underpinned by a strong consensus in Mexico about macroeconomic stability**. Mexico has continued to implement sound macro policies supported by its strong policy frameworks, and the incoming administration has stressed that it is firmly committed to maintaining prudent policies within the current frameworks. Monetary policy will continue to be guided by the inflation targeting framework, in the context of the floating exchange regime; fiscal policy will be anchored by the balanced budget rule; and financial oversight will be based on the sound regulatory and supervisory framework.

9. **With Mexico's economy operating close to potential but external risks looming large, the authorities aim to maintain an appropriate policy stance (from a cyclical perspective) and policy mix (to restore Mexico's fiscal buffers).**

- **Fiscal policy**. Amid heightened global risks, continued consolidation efforts next year would help further rebuild fiscal buffers. Under the baseline scenario, fiscal consolidation in 2013 would turn the primary balance into a slight surplus and return to a balanced budget under the fiscal rule.[4]

- **Monetary policy**. The Central Bank remains judiciously vigilant to risks from the possible persistence of recent supply shocks, domestic cyclical conditions and global headwinds. The authorities stressed that the breach of the inflation target variability interval has primarily been due to temporary supply shocks and that medium-term inflation expectations remain firmly anchored. Nonetheless, they are committed to monitor the determinants of inflation closely in order to adjust monetary policy as necessary to keep inflation in line with the target.

- **Exchange rate**. The exchange rate will continue to play a key buffering role against potential shocks, with rules-based FX intervention limited to smoothing disorderly market conditions. In this context, the authorities, including the incoming

[4] Given the presidential transition, the 2013 budget will be discussed and approved during December 2012.

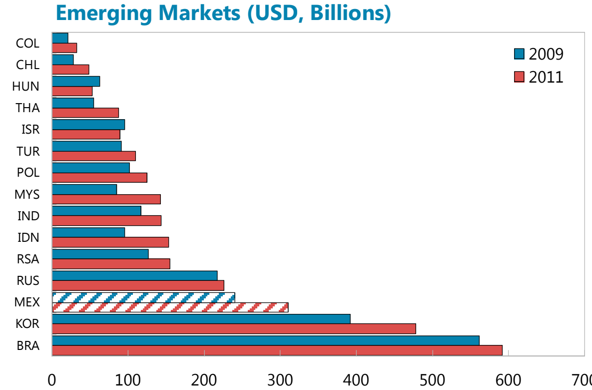
administration, believe that Mexico's level of international reserves appears adequate for normal times but that, amid heightened external uncertainty and Mexico's high integration with international capital markets, the FCL would remain a critical insurance complement against global downside risks.

- **Financial sector**. The authorities will continue to monitor financial sector developments closely, including the subsidiaries of foreign banks and credit segments that have expanded substantially in recent years. Moreover, preparatory work is underway to address recommendations in the recent FSAP Update that require legislative change.

IV. Role of the Flexible Credit Line

10. **Persistent global uncertainty represents a significant risk to Mexico**. Since the approval of the current FCL, downside risks to the global economy have intensified, associated to the potential re-intensification of the euro area crisis due to insufficiently decisive policy action, and the risk of an abrupt tightening of U.S. fiscal policy or uncertainty about raising of the debt ceiling. Increased external uncertainty so far has affected emerging markets transitorily (during the bouts of global risk aversion), but beyond temporary disruptions foreign investor flows have continued. However, if global downside risks were to materialize a surge in global risk aversion and a generalized pull back would be expected to affect the emerging market asset class, particularly those with open capital accounts and liquid financial markets. This risk is particularly relevant for Mexico, given the large and growing foreign portfolio inflows since 2010.

Stock of Non-resident Portfolio Investment in Emerging Markets (USD, Billions)



Sources: IFS

11. **In this context, the authorities continue to see a critical need for insurance against external downside risks, and are requesting a new 2-year FCL arrangement maintaining access at SDR 47.292 billion (about US$73 billion), which they intend to treat as precautionary**. This implies a reduction in quota access from 1,500 percent (originally approved in the current arrangement) to 1,304 percent.[5] Mexico's reserve

[5] Access at 1,304 of quota would carry an annual commitment fee as follows: 15 basis points, if access in a twelve-month period is less than or equal to 200 percent of quota; 30 basis points, if access is between 200 and 1000 percent of quota, and 60 basis points, if access is exceeding 1000 percent of quota (i.e., a total of SDR 164.1 million per annum, or 34.7 basis points).

accumulation over the last two years, in a context of very large capital inflows, has increased reserve coverage moderately, remaining relatively low in terms of balance sheet indicators. While the authorities are expected to continue taking advantage of favorable oil prices to increase their reserve cushion and to maintain an adequate level of reserves for normal times, they consider the FCL a critical pillar against global downside risks. Moreover, the authorities consider that the FCL has successfully supported their macroeconomic strategy amid persistent unsettled external conditions since the global crisis. They stressed the crucial importance of the FCL as a complement to reserves and to reinforce market confidence on Mexico's strong policies and frameworks, particularly at the current juncture.

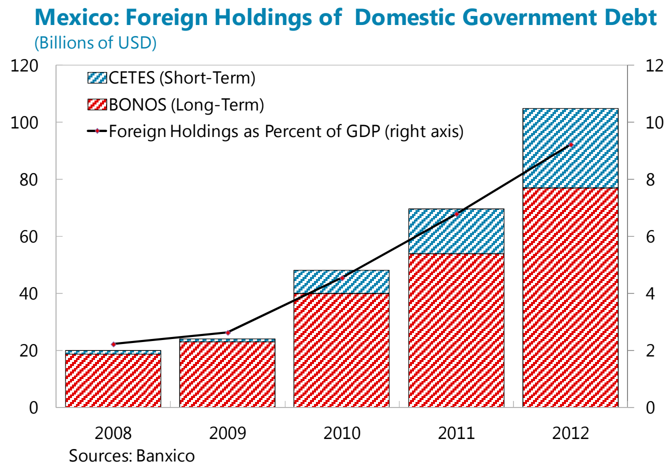
12. **Exit strategy.** While maintaining access in SDR terms, the authorities considered the reduction in quota access as appropriate given the current risk balance. They underscored their intention to take further steps towards exit when improved external conditions allow. The authorities are committed to maintain very strong policies in line with their frameworks and continue the fiscal consolidation efforts, while taking stock of evolving global conditions.

V. ACCESS CONSIDERATIONS

13. **In the context of high and persistent global uncertainty, Mexico's access case rests on its very open capital account and large balance sheet exposures from foreign portfolio investment**. The recognition of Mexico's strong fundamentals and prudent policies have resulted in large capital inflows, particularly after the global crisis and Mexico's inclusion in the World Global Bond Index (WGBI) in 2010. In this context, persistent global uncertainty and heightened downside risks remain material to Mexico, linked to a potential surge in global risk aversion and a generalized pullback from the emerging market asset class, even from strong countries like Mexico. While a gradual reserve accumulation has allowed Mexico to increase external buffers, they remain relatively low in terms of balance sheet exposures that could reverse during global financial distress.

- **As highlighted in the latest WEO and GFSR, global downside risks have intensified, as confidence in the global financial system has become very fragile.** An intensification of the Euro Area crisis represents a major risk, particularly for emerging economies with open capital accounts and liquid financial markets, like Mexico. A materialization of the U.S. fiscal cliff could drive the U.S. economy into a recession and unsettle global financial conditions, with significant spillovers on Mexico.

- **Foreign portfolio exposures in Mexico have increased significantly since the global crisis, particularly in sovereign debt markets.** Increased investor appetite for Mexican assets has been associated with: (i) the recognition of Mexico's strong fundamentals and policy frameworks; (ii) the absence of controls on the capital account and stability of taxes and regulations for foreign investment; and (iii) the liquidity of its sovereign and FX markets. The stock of foreign portfolio investment in Mexico has increased by almost 80 percent during the last three years, from about US$200 billion as of mid-2009 to US$355 billion in mid-2012. Capital inflows have been particularly large in domestic sovereign debt markets where the stock of foreign portfolio holdings increased from about US$20 billion in 2009 to about US$110 billion in 2012, which added to the already significant stock of foreign equity holdings (US$143 billion in 2012). A significant part of portfolio inflows has been from institutional investors into the long-end of the yield curve, driven largely by Mexico's strong fundamentals and its inclusion in the WGBI.[6] More recently, though, flows to short-term government paper (CETES) have increased considerably, driven in part by carry trade operations. Given the impact that a surge in global risk aversion can have on the emerging asset class as a whole, including sound countries like Mexico, the large portfolio exposures represent a significant source of risk under adverse external scenarios.



- **While reserve coverage has increased somewhat since the global crisis, it remains relatively low in terms of balance sheet exposures that could reverse in case of global financial distress.** The increased investor appetite for Mexican assets has meant that the efforts to build up reserve buffers have increased the coverage ratio vis-à-vis foreign portfolio liabilities only modestly since 2009.[7] The coverage of monetary aggregates shows a similar picture, with the increase in

Mexico: Comparisons under various reserve adequacy metrics (end 2011)

	Mexico	Cross-Country Median 1/
	(in percent)	
Reserves to Broad Money	21.2	33.7
Reserves to GDP	12.9	16.6
Reserves to Portfolio Investment	48.2	134.0
Reservest to ARA Metric	130.2	117.8

Source: WEO and IFS
1/ Countries included are: Argentina, Bosnia and Herzegovinia, Brazil, Bulgaria, Chile, China, Colombia, Costa Rica, Croatia, Dominican Rep., Ecuador, Egypt, El Salvador, Guatemala, India, Indonesia, Jamaica, Jordan, Latvia, Lithuania, Malaysia, Morocco, Pakistan, Panama, Peru, Philippines, Poland, Romania, Russia, Serbia, South Africa, Thailand, Tunisia, Turkey, Ukraine, Uruguay, Venezuela.

[6] This increase in investor preference for Mexican assets is seen predominantly as a structural allocation. However, institutional investors can be subject to stop-loss rules, which in periods of high uncertainty and large currency and price volatility can generate perverse market dynamics.

[7] The reserve coverage was 40 percent of portfolio liabilities in 2009.

coverage in this period from 16 to 21 percent of broad money.[8] Both metrics of reserve coverage remain low compared to peer countries. The ARA metric and reserves as months of imports show that Mexico is in line with other emerging market peers. Other metrics show that Mexico has relatively lower coverage than other emerging market peers in the case of reserves to GDP, and larger coverage of short-term debt at residual maturity plus the current account deficit. However, Mexico has low short-term debt and current account deficits, and high correlation between exports and imports, which suggests that less weight should be given to metrics including these variables as indicators of potential external drains.

14. **The main sources of reserve drains in an adverse scenario would stem from the capital account, and in particular portfolio flows (Box 1).** The access case rests on a plausible downside scenario involving primarily a situation of a sudden stop rather than outright divestment of portfolio holdings in secondary markets. In particular, the shocks underpinning the size of potential drains are in line with the current FCL arrangement (except that the present scenario assumes no accumulation of reserves as in the past).

[8] The ratio of reserves to broad money is an indicator of coverage against the risk of capital flight that has been shown to be of particular importance for emerging markets (Maurice Obstfeld, Jay C. Shambaugh, and Alan M. Taylor, 2010. "Financial Stability, the Trilemma, and International Reserves," *American Economic Journal: Macroeconomics*, American Economic Association, vol. 2(2), pages 57–94, April.)

Box 1. Illustrative Adverse Scenario

An illustrative adverse scenario developed by staff suggests possible annual financing gaps of US$73 in 2013 and US$80 billion in 2014. This scenario illustrates the potential impact on Mexico's balance of payments of adverse external shocks associated with a surge in global risk aversion (amplified by slower global growth). The scenario applies independent shocks in 2013 and in 2014 to generate an access envelope.

The shocks in the **2013 adverse scenario** can be summarized as follows (Table A):

Table A. Mexico: Adverse Scenario

Potential sources of drain:		Shocks in the Adverse Scenario, 2013 (in billions of dollars)	(in standard deviations) 2/
Current account		**-9.8**	1.1
o/w Oil trade balance		-2.7	1.0
Non-factor services balance		-2.6	2.0
Net transfers (Remittances)		-4.5	2.2
Net Foreign Direct Investment		**-9.5**	1.5
Gross Portfolio Investment in Domestic Market		**-37.5**	
Foreigners' Investment in Domestic Sovereign Bonds 3/		-30.0	1.8
Foreigners' Equity Holdings		-7.5	1.9
Cushion built in FCL access		0.0	.
Private and Public External Financing (Bonds and Loans)		**-11.0**	1.8
Residents' investment outflows (portfolio and other)		**-21.0**	1.5
Total Sources of Drain		**-88.8**	
Drawdown of Reserves Accumulated under the Baseline		16.0	
Potential Financing Gap	In billion dollars	**-72.8**	
	In bilions of SDRs	**47.3**	
Memo item:			
Reserve Accumulation		0 percent of baseline	

- C**urrent account**. The current account is assumed to deteriorate, reflecting: (i) a 20 percent fall in oil prices; (ii) a negative shock to the non-factor services balance; and (iii) a drop in remittances similar to the one observed in 2009. Weaker external demand is assumed to have a small impact on the non-oil trade balance, given the high import content of Mexico's exports.
- **Net foreign direct investment**. Global economic and financial distress is assumed to cause FDI to decline, although by about half of the fall in 2008–2009 (since FDI flows are yet to recover to their pre-crisis levels).

[1/] Standard deviations for each BOP component are calculated on annual changes since the mid-1990s. The magnitude of the shocks in terms of standard deviations indicates that this is a plausible adverse scenario.

[2/] Standard deviation calculated for 2009 onwards, using annualized quarterly data, as foreign holdings of domestic government paper have increased sharply in recent years (from about US$20 billion in 2009 to almost US$110 billion in 2012, or 32 of the total stock). Using data before 2009 would underestimate the relevant standard deviation for the scenario.

Box 1. Illustrative Adverse Scenario (continued)

- **Public external financing.** Reflecting their prudent debt management and their strong track-record of securing external access, the authorities secure financing covering 86 percent of debt coming due.

- **Foreigners' investments in domestic sovereign bond markets.** Rollover of sovereign debt by foreign investor is assumed to fall to 90 percent for short-term paper, and 80 percent for long-term instruments.[3/]

- **Foreign equity outflows.** Equity sales represent approximately 5 percent of the total stock of equity portfolio liabilities held by non-residents, similar to the experience during the global crisis.

Table B. Roll-Over Rates (in percent)

	Adverse Scenario-2013
Private ST	90
Private MLT	95
Public ST 1/	90
Public MLT 2/	85

1/ Local bond issuances in pesos.
2/ Local bond issuances in pesos and external issuances in dollars.

- **Private sector FX medium and long-term issuances.** The adverse scenario assumes lower bond placements in international markets and rollover rates above 95 percent.

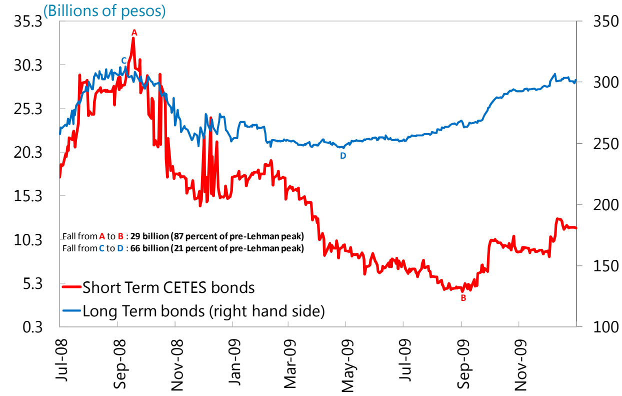
- **Short-term private external financing.** This is mostly associated with a reduction in foreign banks cross-border lending, with a rollover rate at 89 percent.

- **Resident investments outflows.** These flows have been sizeable and volatile in the past, and the scenario assumes an increase in residents' assets abroad, mostly in the form of portfolio investments.

Assumptions in the adverse scenario are plausible compared with Mexico's experience during the global crisis. The reduction in the stock of foreign holdings of short-term and long-term domestic public bonds—as percent of the total stock—are below those observed during 2008–2009 (Figure A). The assumptions about changes in residents' investment abroad and FDI (US$21 billion and US$10 billion) are also below those experienced during the crisis (US$45 billion and US$18 billion), while assumptions on foreign equity portfolio investment are in line with the global crisis (Figures B and C).

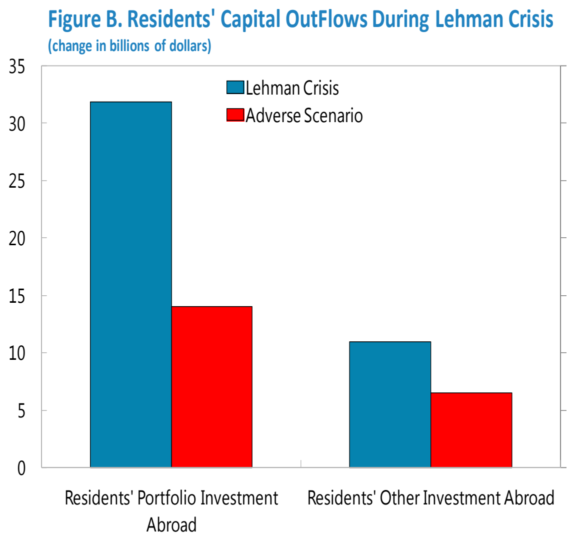
Figure A. Foreigners' Holdings of Mexican Domestic Government Bonds around the Global Crisis 2008-2009

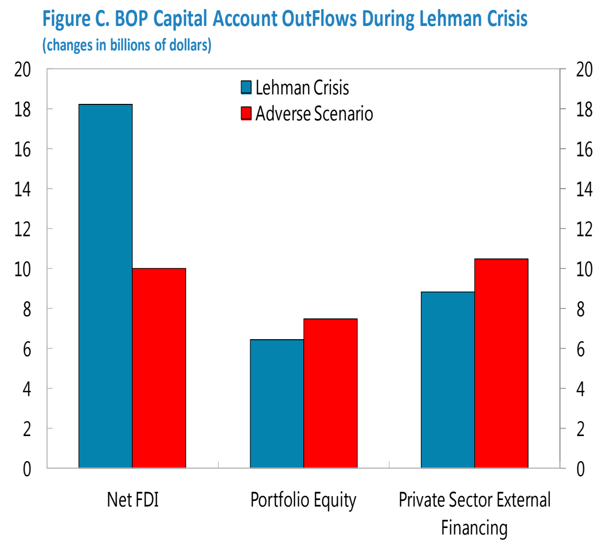
(Billions of pesos)



[3/] For a comparison of rollover rates in this scenario with those assumed in previous FCLs, see Appendix 1.

Box 1. Illustrative Adverse Scenario (continued)





This current adverse scenario is broadly in line with that presented for the 2011 FCL (Table C), with two exceptions: (i) the present adverse scenario assumes no accumulation of international reserves, in contrast to the buildup assumed in the past; and (ii) the current scenario calibrates in more detail the potential outflows associated with portfolio investment, rather than including a generic buffer.

Table C. Mexico: Comparison between Current Adverse Scenario and 2011 FCL Scenario
(in billions of dollars, except where noted)

Potential sources of drain:		Adverse Scenario, 2013	2011 FCL
Current account		**-9.8**	**-7.2**
Net Foreign Direct Investment		**-9.5**	**-8.2**
Financial Capital Flows		**-69.0**	**-58.4**
Foreigners' Investment in Domestic Sovereign Bonds		-30.0	-5.6
Foreigners' Equity Holdings		-7.5	0.0
Private and Public External Financing and Residents' Outflows		-31.5	-23.8
Cushion built in FCL access		0.0	-27.5
Total Sources of Drain		**-88.3**	**-72.3**
Drawdown of Reserves Accumulated under the Baseline		16.0	0
Potential Financing Gap	In billion dollars	**-72.8**	**-72.3**
	In bilions of SDRs	47.3	47.3
Memo item:			
Reserve Accumulation		0 percent of baseline	100 percent of baseline

Box 1. Illustrative Adverse Scenario (concluded)

For 2014, the adverse scenario is built on the higher stock of foreign portfolio liabilities in 2013 under the baseline of no shock that year (assuming the same shocks in terms of standard deviations) and lower baseline reserve accumulation (Table D).

Table D. Mexico: Baseline and Adverse BOP Scenarios
(in billions of dollars)

		2013			2014		
Potential sources of drain:	2012	Baseline	Shocks	Adverse Scenario	Baseline	Shocks	Adverse Scenario
Current account	-11.1	-13.5	-9.8	-23.3	-14.7	-9.8	-24.5
Trade Balance	-0.7	-3.2	-2.7	-5.9	-5.2	-2.7	-7.9
o/w Oil balance	10.7	10.4	-2.7	7.7	8.4	-2.7	5.7
Non-factor services balance	-14.4	-14.6	-2.6	-17.2	-15.0	-2.6	-17.6
Factor services balance	-19.4	-19.7	0.0	-22.3	-19.4	0.0	-19.4
Net transfers (Remittances)	23.4	24.0	-4.5	19.5	24.8	-4.5	20.3
Net Foreign Direct Investment	13.2	12.9	-9.5	3.4	14.2	-9.5	4.7
Gross Portfolio Investment in Domestic Market	43.2	27.8	-37.5	-9.7	20.0	-40.5	-20.5
Foreigners' Investment in Domestic Sovereign Bonds	40.9	25.3	-30.0	-4.7	17.4	-33.0	-15.6
Foreigners' Equity Holdings	2.3	2.4	-7.5	-5.1	2.5	-7.5	-5.0
Private External Financing (bonds, loans and trade finance)	-1.3	-3.0	-10.0	-13.0	0.6	-10.0	-9.4
Short-term	-2.3	-4.4	-8.0	-12.4	-1.4	-8.0	-9.4
Medium and Long-term	1.0	1.4	-2.0	-0.6	2.0	-2.0	0.0
Public Financing Abroad (Bonds and Loans)	-1.9	-1.0	-1.0	-2.0	-1.0	-1.0	-2.0
Residents' investment outflows (portfolio, deposits and real assets)	-6.1	-7.1	-21.0	-28.1	-7.1	-21.0	-28.1
Errors and Omissions and valuation effects	-15.0	0.0	0.0	0.0	0.0	0.0	0.0
Total Sources of Drain			**-88.8**			**-91.8**	
Reserve Accumulation	**21.0**	**16.0**		**-72.8**	**12.0**		**-79.8**
Memo item:							
Reserve Accumulation under Adverse Scenario			0 percent of baseline			0 percent of baseline	

VI. Review of Qualification

15. **The staff assesses that Mexico continues fully to meet the qualification criteria for an arrangement under the FCL** (Figure 6). The authorities have in place very strong policy frameworks, which include monetary policy guided by an inflation targeting framework in the context of a flexible exchange regime, fiscal policy anchored by a balanced budget rule and financial oversight based on a sound regulatory and supervisory framework. The incoming administration is firmly committed to maintaining Mexico's strong policy frameworks and prudent policies, which they have explicitly endorsed in the letter accompanying the authorities' letter. At the conclusion of the 2012 Article IV Consultation,

Executive Directors commended the authorities for Mexico's strong rules-based policy framework and their skillful macroeconomic management.

- **Sustainable external position.** The current account deficit is small and is envisaged to remain moderate over the medium term, while the exchange rate remains broadly in line with fundamentals. The updated external debt sustainability analysis (Figure 7) continues to show that Mexico's external debt remains moderate and is expected to fall over the medium term, even in the presence of potential shocks.

- **Capital account position dominated by private flows.** The bulk of Mexico's external debt continues to be owed to private creditors, and private portfolio flows (debt and non-debt creating) and FDI continue to be large relative to overall balance of payments flows.

- **Track-record of steady sovereign access to international capital markets at favorable terms.** Mexico is among the highest-rated emerging markets and its sovereign spreads remain low at about 125 basis points (compared to 260 basis points on average for emerging economies), while CDS spreads (at around 100 basis points) are close to the historical minimum reached in 2008. Moreover, taking advantage of favorable market conditions, Mexico has continued to improve its debt profile, successfully placing sovereign longer-dated bonds in international capital markets at historically low yields.[9]

- **Relatively comfortable reserve position.** Gross international reserves reached US$166 billion by end-September, about US$16 billion above the level of end-2011. As assessed in the recent Article IV consultation, this level of reserves is relatively comfortable according to standard reserve adequacy indicators (see Figure 8).

- **Sustainable public debt position and sound public finances.** Fiscal policy remains guided by the balanced budget rule, which underpins the authorities' commitment to keep the augmented public sector deficit at a level that ensures overall public sector debt sustainability. The authorities have pursued a gradual fiscal consolidation after the fiscal stimulus put in place during the global crisis, which attests to their strong track record of policies to maintain sound public finances. The updated debt sustainability analysis continues to show a gradual decline in the public debt to GDP ratio and indicates that the debt trajectory is broadly robust to most standard shocks

[9] This year the authorities have issued US$4 billion of 10-year and 32-year bonds in international capital markets, at yields of 3.71 percent (the lowest yield on record for Mexico) and 4.84 percent respectively (with a coupon of 4.75 percent, the lowest obtained by a Latin American sovereign issuing bonds at that maturity in US dollars). The authorities also placed a Samurai-bond for ¥80 billion (US$1 billion) in May. In July, Mexico placed 30-year MBono in domestic markets (in pesos) at yields of around 6¼ percent.

(Figure 9). The fiscal outlook is sensitive to growth dynamics and the evolution of oil revenues, but the balanced budget rule provides assurances of fiscal sustainability.

- **Low and stable inflation**. Inflationary pressures remain contained, despite the recent uptick in headline inflation linked to higher food prices. Core inflation remains within the inflation target variability interval, particularly in services, indicating limited demand pressures. Headline inflation developments are viewed as temporary and supply-driven, with medium-term inflation expectations remaining firmly anchored.

- **Absence of systemic bank solvency problems that pose an immediate threat of a banking crisis.** The recent FSAP Update found that Mexico's banking system remains sound, with good levels of liquidity, capital, and profitability. The authorities are planning to implement most Basel III capital requirements by next January, as most banks already have sufficient high quality capital to meet the 2019 ratio for capital plus conservation buffer of 10½ percent. Mexico's banking system has remained resilient to the effects of unsettled market conditions in Europe.

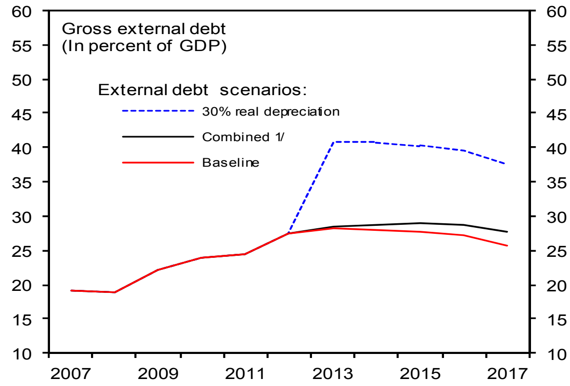
- **Effective financial sector supervision.** The FSAP Update also concluded that Mexico's overall financial sector supervision framework is effective, and that the institutional set-up for macro-financial oversight and systemic crisis management has been strengthened with the establishment of the Financial System Stability Council. The authorities have taken steps to address portfolio concentration issues including by tightening rules on relevant party transactions and applying concentration limits on bank loans to subnational governments that are not guaranteed by federal transfers. Preparatory work is advanced to address FSAP recommendations that require legislative change.

- **Data transparency and integrity.** The overall quality of Mexican data continues to be adequate for surveillance as described in the October 2010 data ROSC Update. Mexico remains in observance of the Special Data Dissemination Standards (SDDS).

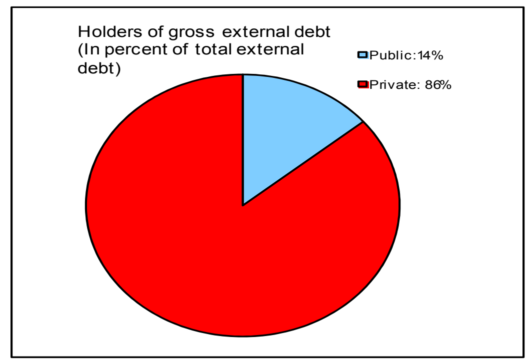
16. **The authorities' letter, endorsed by the incoming administration, attests to their continued commitment to very strong policy frameworks and implementing sound macroeconomic policies.** The authorities underscore their continued commitment to implement prudent policies underpinned by Mexico's strong policy frameworks, and point to the fact that policy continuity is firmly anchored on a broad consensus in Mexico in support of macroeconomic stability. The incoming administration has explicitly endorsed the authorities' letter, highlighting that it remains firmly committed to maintaining prudent policies within the current frameworks. See Attachments 1 and 2.

Figure 6. Mexico: Qualification Criteria

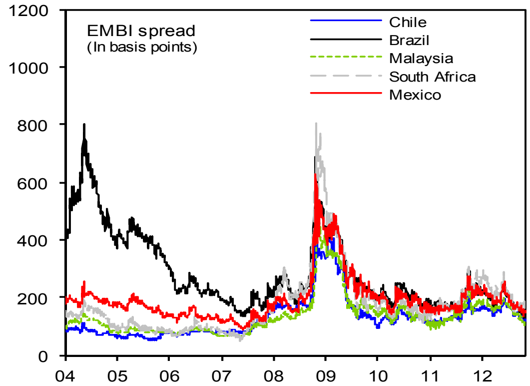
Sustainable external position



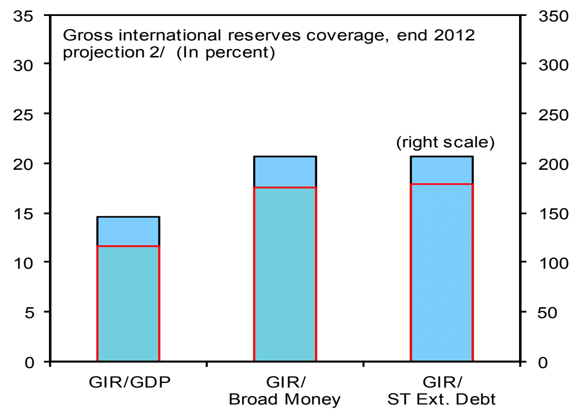
Almost all external debt to private creditors



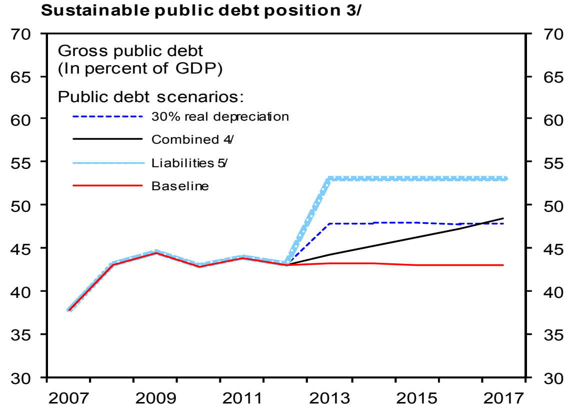
Steady sovereign capital markets access



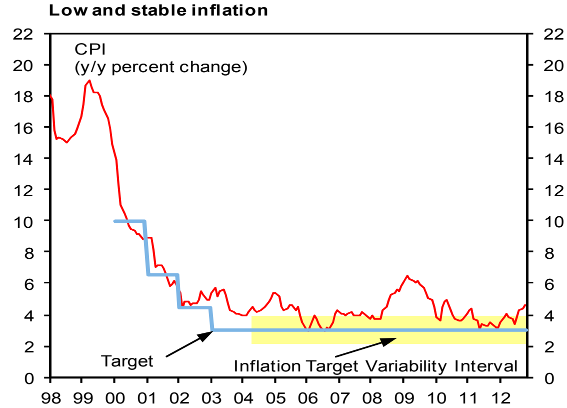
Relatively comfortable reserve coverage



Sustainable public debt position 3/

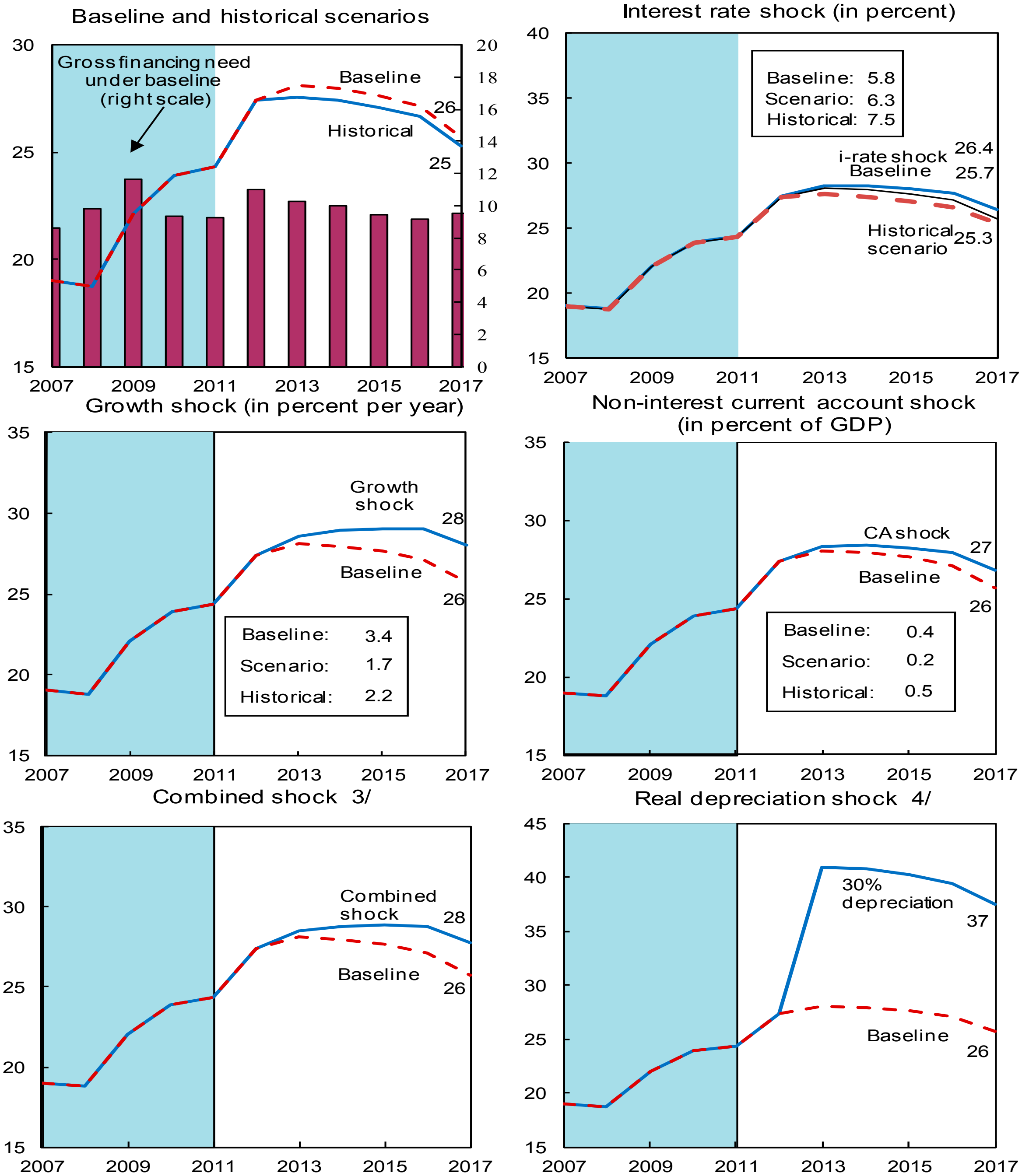


Low and stable inflation



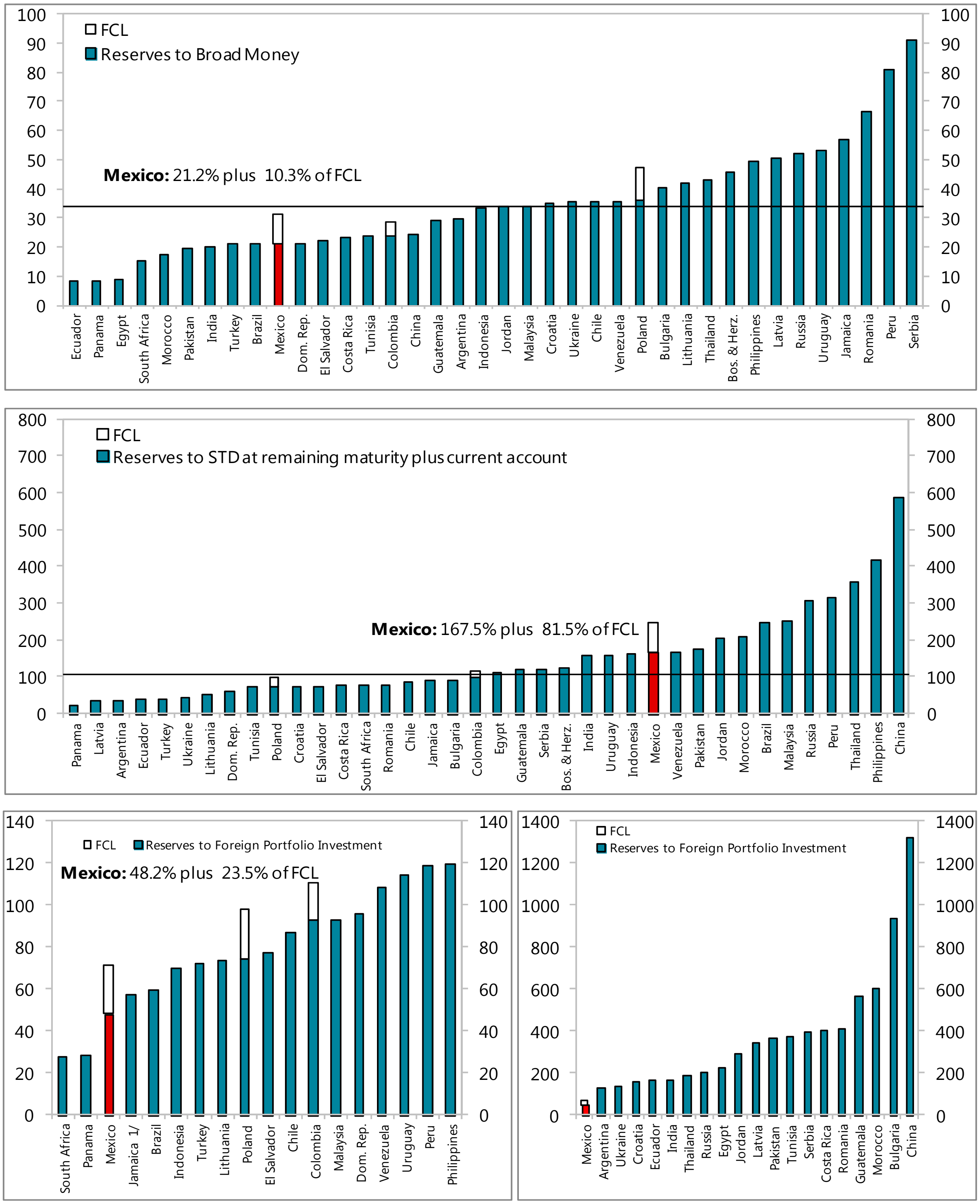
Sources: Bloomberg L.P.; Datastream; EMED; Haver Analytics; and IMF staff calculations.
1/ Combined permanent 1/4 standard deviation shocks applied to interest rate, growth, and primary current account balance.
2/ Red bar shows ratio for end-year 2010, when FCL was approved.
3/ Not taking into account offsetting measures required under the balance budget rule.
4/ Combined permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.
5/ One-time 10 percent of GDP increase in debt-creating flows.

Figure 7. Mexico: External Debt Sustainability: Bound Tests 1/ 2/
(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
4/ One-time real depreciation of 30 percent occurs in 2012.

Figure 8. Mexico: Metrics of Reserve Coverage in a Cross-Country Perspective, 2011

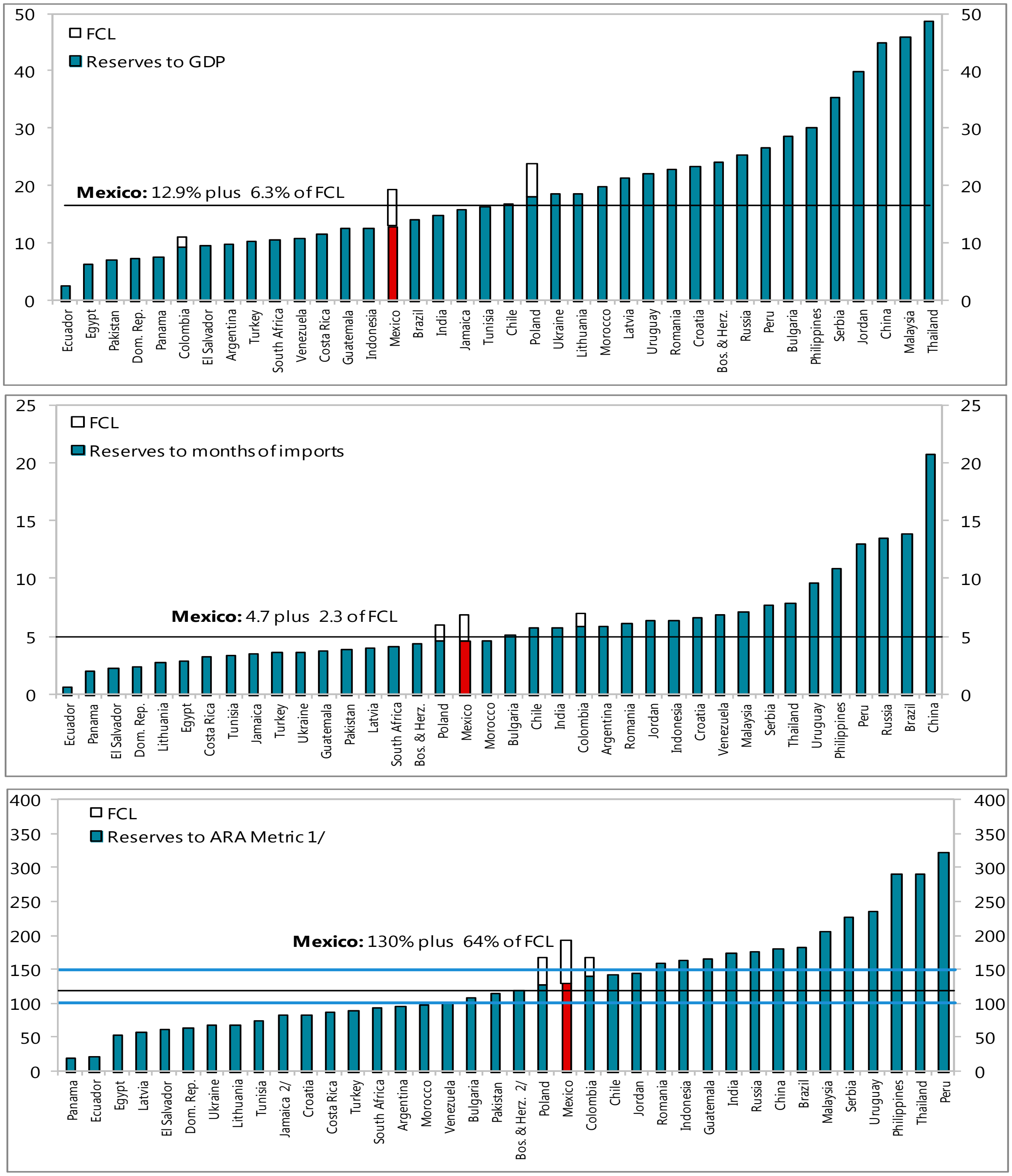


Sources: World Economic Outlook, and IMF staff estimates.

1/ Portfolio liabilities only available until 2010.

Note: Black line represents the cross-country median.

Figure 8. Mexico: Metrics of Reserve Coverage in a Cross-Country Perspective, 2011 (concluded)



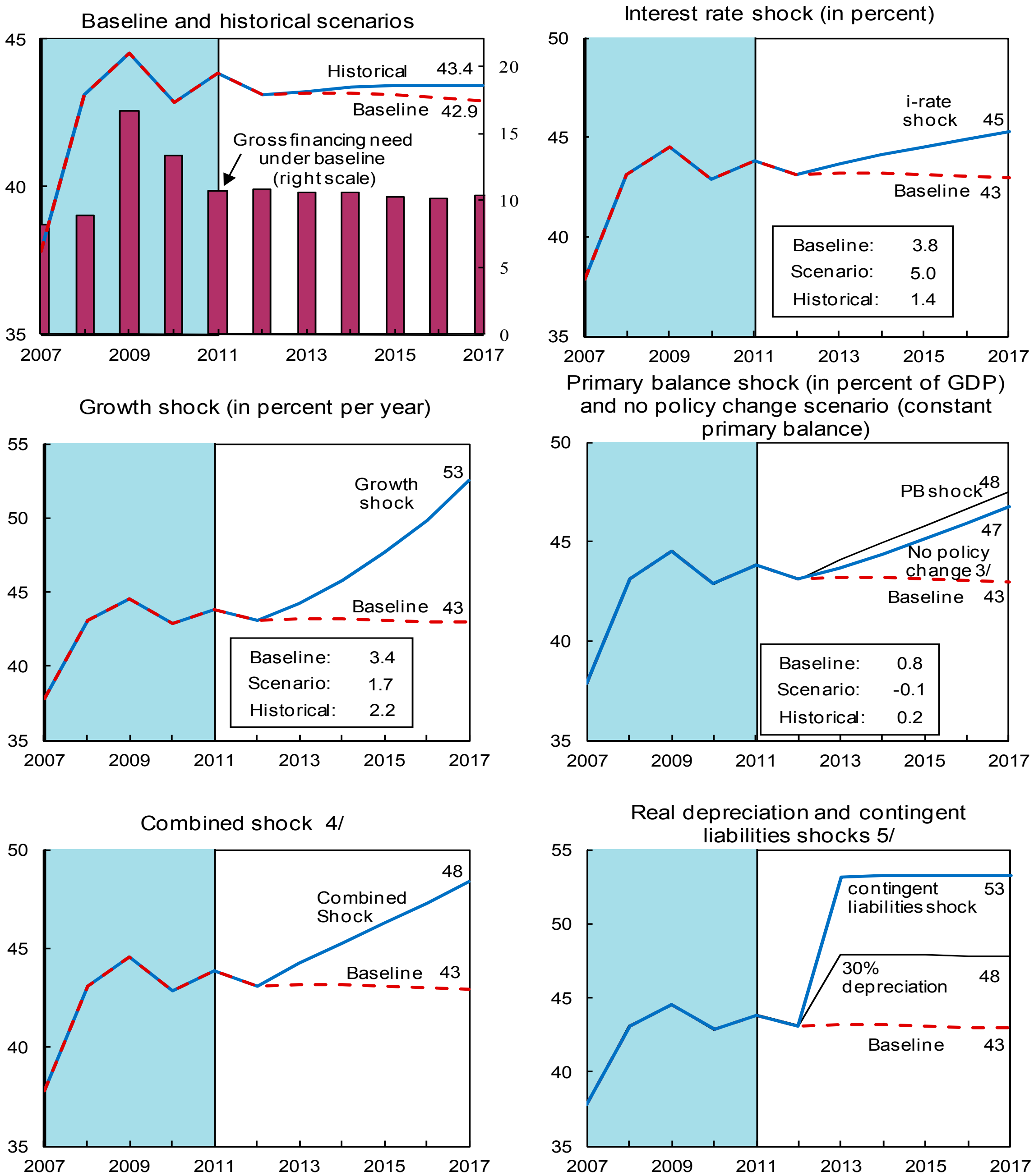
Sources: World Economic Outlook, Balance of Payments Statistics Database, and IMF staff estimates.

1/ The ARA metric was developed by the Strategy and Policy Review Department to assess reserve adequacy. The blue lines denote the 100-150 percent range of reserve coverage regarded as adequate for a typical country under this metric.

2/ Portfolio liabilities only available until 2010.

Note: Black line represents the cross-country median.

Figure 9. Mexico: Public Debt Sustainability: Bound Tests 1/ 2/
(Public debt in percent of GDP)



Sources: International Monetary Fund, country desk data, and staff estimates.
1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.
3/ This mechanical exercises assumes that the budget rule does not hold.
4/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.
5/ One-time real depreciation of 30 percent and 10 percent of GDP shock to contingent liabilities occur in 2010, with real depreciation defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

VII. Impact on Fund Finances, Risks, and Safeguards

17. **Access under the proposed FCL for Mexico of 1,304 percent of quota (SDR 47.292 billion) is large, but the impact on Fund liquidity and the risks to the Fund are manageable**. As with the current arrangement, if drawn, the proposed FCL arrangement would become the Fund's largest single credit exposure. However, the Fund's liquidity is expected to remain adequate after the approval of the proposed FCL arrangement for Mexico, as further discussed in the supplement assessing the impact on the Fund's finances and liquidity position.

18. **Notwithstanding the large size of the commitment, the risks to the Fund are judged to be low**. The authorities have given clear indications that they intend to treat the arrangement as precautionary. Even if a full drawing under the arrangement were to be made on approval, Mexico's external debt would remain moderate at about 26¼ percent of GDP in 2017, when debt service peaks (Table 7). Further, even peak debt service ratios would be broadly in line with those in recent years, and remain well within the range seen in other emerging market countries. Moreover, Mexico has a demonstrated excellent track record of meeting its obligations to the Fund.

19. **Staff completed the safeguards procedures applicable to FCL arrangements for the current FCL approved in January 2011**. Under these procedures, staff reviews the most recent independent external audit of the member's central bank. The authorities provided the necessary authorization for staff to communicate directly with the Banxico's external auditor, PricewaterhouseCoopers (PwC) Mexico. PwC issued an unqualified audit opinion on the Banxico's 2010 financial statements in March 2011. Staff has reviewed the 2010 audit results and discussed them with PwC on September 8, 2011. No significant safeguards issues emerged from the conduct of these procedures. Banxico publishes only its balance sheet and audit opinion as part of the annual report. In light of Mexico's request for a successor FCL, Banxico provided the authorizations needed for similar safeguards procedures to be conducted by Fund staff in line with the specific safeguards requirements for FCL arrangements.

VIII. Staff Appraisal

20. **The FCL arrangement for Mexico has provided significant insurance against external downside risks, contributing to maintaining orderly financial market conditions amid persistent unsettled external conditions.** The lowered perception of risks, along with skillful policy management, has been instrumental in Mexico's rapid recovery after the global financial crisis and in reinforcing Mexico's resilience during the recurrent bouts of global risk aversion.

21. **The staff's assessment is that Mexico continues to meet the qualification criteria for access to FCL resources**. Mexico has very strong policy frameworks and economic fundamentals. The authorities have also demonstrated a sustained track record of excellent

policy implementation. The incoming administration is firmly committed to maintaining Mexico's strong policy frameworks and prudent policies, which they have explicitly endorsed in the letter accompanying the authorities' letter.

22. **The staff recommends approval of an FCL arrangement for Mexico of SDR 47.292 billion for a period of 24 months.** Highly unsettled global conditions have persisted since the approval of the previous FCL arrangement, with heightened downside risks for Mexico in the context of its open capital account and liquid financial markets. The new FCL arrangement would continue to support the authorities' overall macroeconomic strategy and bolster Mexico's external buffers. The authorities considered the reduction in quota access as appropriate given the current risk balance. They underscored their intention to take further steps towards exit when improved external conditions allow.

23. **The staff judges the risks to the Fund arising from any potential drawing under the proposed FCL arrangement as low**. The authorities have an excellent policy implementation track record. Their letter reaffirms their commitment to maintain Mexico's very strong policy frameworks and to take needed actions to manage unforeseen risks. Together, these provide a strong assurance that the authorities would react appropriately to any future balance of payments difficulties. Risks to the Fund are further contained by the authorities' intent to treat the FCL arrangement as precautionary, Mexico's very strong repurchase record with the Fund, as well as the manageable external debt service profile even if the full amount of the FCL were to be drawn up-front.

Table 1. Mexico: Selected Economic, Financial, and Social Indicators, 2008–2013

I. Social and Demographic Indicators

GDP per capita (U.S. dollars, 2011)	10,161.1	Poverty headcount ratio (% of population, 2010) 1/	51.3
Population (millions, 2011)	113.7	Income share of highest 20 percent / lowest 20 percent	11.3
Life expectancy at birth (years, 2012)	75.6	Adult illiteracy rate (2011-2012)	6.4
Infant mortality rate (per thousand, 2012)	13.2	Gross primary education enrollment rate (2010)	114.1

II. Economic Indicators

	2008	2009	2010	2011	Proj. 2012	Proj. 2013
(Annual percentage change, unless otherwise indicated)						
National accounts in constant prices						
Real GDP	1.2	-6.0	5.6	3.9	3.8	3.5
Net exports (contribution)	-0.7	2.1	0.0	-0.1	0.1	0.2
Total domestic demand	1.8	-7.8	5.4	3.9	3.6	3.4
o/w Consumption	1.6	-5.8	4.6	3.9	3.5	3.7
Gross fixed investment	5.5	-11.8	6.2	8.9	5.0	5.0
External sector						
Exports of goods, f.o.b.	7.2	-21.2	29.9	17.1	7.4	5.8
Export volume	-2.4	-7.7	15.8	2.2	7.4	6.2
Imports of goods, f.o.b.	9.5	-24.0	28.6	16.4	7.0	6.4
Import volume	1.0	-21.0	23.3	8.5	7.2	7.1
Petroleum exports (percent of total exports of goods)	17.4	13.4	14.0	16.1	15.2	14.2
Terms of trade (deterioration -)	1.3	-11.2	7.6	6.8	0.1	0.2
Exchange rates						
Nominal exchange rate (US$/Mex$)						
(average, depreciation -)	-1.8	-17.6	6.9	1.7	-7.9	...
Real effective exchange rate (CPI based)						
(average, depreciation -)	-1.6	-12.4	8.6	0.4	-5.1	-0.7
Employment and inflation						
Consumer prices (annual average)	5.1	5.3	4.2	3.4	4.1	3.5
Formal sector employment, IMSS-insured workers (annual average) 2/	2.1	-3.1	3.8	4.3	3.3	...
National unemployment rate (annual average)	4.0	5.5	5.4	5.2	4.8	...
Unit labor costs: manufacturing (real terms, annual average) 2/	2.5	1.1	-7.3	-1.4	-3.3	...
Money and credit						
Bank credit to non-financial private sector (percent growth)	13.5	-1.0	10.0	17.2	15.9	14.5
Broad money (M4a)	16.8	6.1	12.0	15.7	15.3	10.7
Treasury bill rate (28-day cetes, in percent, annual average)	7.7	5.4	4.4	4.2	4.4	...
(In percent of GDP)						
Nonfinancial public sector						
Government revenue	23.5	23.6	22.6	22.8	23.1	23.2
Government expenditure	23.6	25.9	25.5	25.3	25.4	25.1
Traditional balance 3/	-0.1	-2.3	-2.8	-2.5	-2.4	-1.9
Augmented balance 4/	-1.1	-4.7	-4.3	-3.4	-2.6	-2.1
Gross public sector debt	43.1	44.5	42.9	43.8	43.1	43.2
Net public sector debt	33.4	36.7	36.8	38.0	37.8	37.7
Savings and investment						
Gross domestic investment	26.9	23.7	24.0	25.1	24.9	25.3
Public	5.6	6.1	6.1	5.9	5.5	5.2
Private	16.5	15.2	14.5	15.2	16.3	16.9
Gross domestic saving	25.3	23.2	23.6	24.1	24.0	24.2
Public 5/	4.1	0.9	1.3	2.0	2.5	2.6
Private	21.3	22.3	22.3	22.1	21.5	21.7
External current account balance	-1.6	-0.6	-0.4	-1.0	-1.0	-1.1
Non-oil external current account balance	-2.9	-1.7	-1.5	-2.1	-1.9	-1.9
Net foreign direct investment	2.4	0.9	0.4	0.8	1.1	1.1
Net portfolio investment	0.4	1.7	3.6	3.5	3.6	2.3
Memorandum items						
Gross external debt (in percent of GDP, end of period)	18.6	22.0	23.9	24.3	27.4	28.1
Total external debt service (in percent of exports and other FX income)	6.8	6.7	4.8	6.5	5.9	5.5
Crude oil export price, Mexican mix (US$/bbl)	84.4	57.4	72.3	101.0	103.1	102.1

Sources: World Bank Development Indicators; CONEVAL; National Institute of Statistics and Geography; National Council of Population; Bank of Mexico; Secretariat of Finance and Public Credit; and IMF staff estimates.

1/ Broadest national definition (CONEVAL).
2/ 2012 based on data available until June 2012.
3/ Authorities' definition. The break in the series in 2009 is due to definitional and accounting changes of PIDIREGAS.
4/ Federal Government plus Social Security and State-owned Companies, excl. nonrecurring revenue and transfers to stabilization funds.
5/ Estimated as the difference between the augmented fiscal balance, as reported by SHCP, and public investment, as reported in the national accounts.

Table 2. Mexico: Financial Operations of the Public Sector, 2008–2017

(In percent of GDP)

	2008	2009	2010	2011	2012 Proj.	2013 Proj.	2014 Proj.	2015 Proj.	2016 Proj.	2017 Proj.
Budgetary revenue, by type	**23.5**	**23.6**	**22.6**	**22.8**	**23.1**	**23.2**	**23.2**	**23.5**	**23.0**	**22.6**
Oil revenue	8.6	7.7	7.3	7.5	7.9	8.2	8.4	8.7	8.3	7.9
Non-oil tax revenue 1/	10.0	9.6	10.2	10.2	10.1	10.0	9.8	9.8	9.7	9.7
Non-oil non-tax revenue	4.9	6.3	5.1	5.1	5.0	5.0	5.0	5.0	5.0	5.0
Budgetary revenue, by entity	23.5	23.6	22.6	22.8	23.1	23.2	23.2	23.5	23.0	22.6
Federal government revenue	16.8	16.8	15.9	16.2	16.7	17.2	17.8	18.6	18.3	18.1
Tax revenue, *of which:*	8.2	9.5	9.6	9.0	9.1	9.4	9.8	10.4	10.4	10.5
excises (including fuel)	-1.4	0.4	0.0	-0.5	-0.4	-0.1	0.5	1.2	1.2	1.3
Nontax revenue	8.7	7.3	6.3	7.2	7.6	7.8	8.0	8.2	7.9	7.6
Public enterprises	6.7	6.8	6.7	6.6	6.3	6.0	5.4	4.9	4.7	4.5
PEMEX	3.0	3.2	2.9	2.8	2.7	2.4	1.8	1.2	1.0	0.9
Other	3.7	3.6	3.8	3.9	3.6	3.6	3.6	3.6	3.6	3.6
Budgetary expenditure	**23.6**	**25.9**	**25.5**	**25.3**	**25.4**	**25.1**	**25.0**	**25.2**	**24.7**	**24.3**
Primary	21.7	23.7	23.5	23.4	23.4	23.0	22.8	22.8	22.3	21.9
Programmable	18.2	20.4	20.0	20.0	19.8	19.3	19.0	18.9	18.4	18.0
Current	13.8	15.3	15.0	15.0	15.1	15.0	14.9	14.8	14.7	14.6
Wages	5.8	6.4	6.1	6.0	6.0	5.9	5.8	5.7	5.6	5.5
Pensions	2.1	2.4	2.6	2.7	2.8	2.9	3.0	3.1	3.2	3.3
Subsidies and transfers	2.6	2.9	2.9	3.1	3.1	3.1	3.1	3.1	3.1	3.1
Other	3.3	3.6	3.4	3.3	3.3	3.1	3.0	2.9	2.8	2.7
Capital	4.4	5.1	5.0	4.9	4.7	4.3	4.1	4.1	3.7	3.4
Physical capital	3.1	4.6	4.8	4.5	4.3	3.9	3.7	3.8	3.5	3.2
Of which: non Pemex	*2.5*	*2.5*	*2.7*	*2.6*	*2.4*	*2.0*	*1.9*	*2.1*	*1.8*	*1.5*
Financial capital 2/	1.3	0.5	0.3	0.4	0.4	0.4	0.3	0.3	0.2	0.2
Nonprogrammable	3.6	3.3	3.5	3.5	3.6	3.7	3.8	4.0	3.9	3.9
Of which: revenue sharing	3.5	3.1	3.3	3.3	3.4	3.5	3.6	3.8	3.8	3.7
Interest payments 3/	1.9	2.2	2.0	1.9	2.1	2.1	2.2	2.3	2.4	2.4
Traditional balance 4/	**-0.1**	**-2.3**	**-2.8**	**-2.5**	**-2.4**	**-1.9**	**-1.8**	**-1.7**	**-1.7**	**-1.7**
Traditional balance for balanced budget rule	0.5	-0.2	-0.8	-0.5	-0.4	0.0	0.0	0.0	0.0	0.0
Adjustments to the traditional balance	**1.0**	**2.4**	**1.5**	**0.9**	**0.2**	**0.2**	**0.2**	**0.3**	**0.3**	**0.3**
PIDIREGAS	1.1	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
IPAB	0.2	0.1	0.1	0.1	0.2	0.2	0.2	0.2	0.2	0.2
Budgetary adjustments	0.3	0.3	0.5	0.2	0.2	0.2	0.2	0.2	0.2	0.2
PEMEX, oil stabilization fund, FARP (-: net inflows)	-1.0	0.7	0.4	0.0	-0.4	-0.4	-0.3	-0.3	-0.2	-0.2
FARAC/FONADIN	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Debtor support	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Development banks (changes in capital)	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Nonrecurring revenue	0.5	1.3	0.4	0.7	0.3	0.3	0.3	0.3	0.3	0.3
Augmented balance 5/	**-1.1**	**-4.7**	**-4.3**	**-3.4**	**-2.6**	**-2.1**	**-2.0**	**-2.0**	**-2.0**	**-2.0**
Augmented interest expenditure 6/	2.5	2.7	2.6	2.4	2.6	2.6	2.7	2.8	2.9	2.9
Augmented primary balance	1.4	-1.9	-1.8	-1.0	0.0	0.5	0.7	0.8	0.9	0.9
Memorandum items										
Crude oil export price, Mexican mix (US$/bbl)	84	57	72	101	103	102	98	94	90	86
Development banks (net lending)	0.4	0.5	0.3	0.4	0.4	0.4	0.4	0.4	0.4	0.4
Non-oil augmented balance 7/	-9.0	-9.5	-9.1	-9.2	-8.7	-8.1	-7.7	-7.4	-7.0	-6.5
Non-oil augmented balance excluding development banks	-8.6	-9.0	-8.8	-8.8	-8.3	-7.7	-7.3	-7.0	-6.6	-6.1
Oil augmented balance	7.4	4.3	4.3	5.3	5.6	5.5	5.2	4.9	4.4	4.0
Structural Primary Fiscal Balance	0.3	-1.6	-1.9	-1.5	-0.5	0.2	0.5	0.8	0.9	1.0
Fiscal Impulse 8/	0.0	1.9	0.3	-0.4	-1.0	-0.7	-0.4	-0.2	-0.1	-0.1
Gross public sector debt	43.1	44.5	42.9	43.8	43.1	43.2	43.2	43.1	43.0	42.9
o/w Domestic (percentage of total debt)	70.3	73.0	76.7	75.5	75.4	76.8	77.9	79.0	80.0	81.1
Net public sector debt	33.4	36.7	36.8	38.0	37.8	37.7	37.7	37.6	37.5	37.5
Nominal GDP (billions of Mexican pesos)	12,176	11,930	13,084	14,336	15,667	16,713	17,819	18,968	20,204	21,503

Sources: Mexican authorities; and IMF staff estimates. Data refer to non-financial public sector, including PEMEX and other public enterprises but excluding state and local governments (except as noted).

1/ Total tax revenue excluding excise tax on gasoline.
2/ Includes transactions in financial assets and capital transfers.
3/ Includes transfers to IPAB and the debtor support programs.
4/ The break in the series in 2009 is due to definitional and accounting changes.
5/ Public Sector Borrowing Requirements excl. nonrecurrent revenue.
6/ Treats transfers to IPAB as interest payments.
7/ Excludes oil revenue (oil extraction rights, PEMEX net income, oil excess return levies, excise tax on gasoline) and PEMEX operational expenditure, interest payments, and capital expenditure.
8/ Negative of the change in the structural primary fiscal balance, measured adjusting tax revenue for the cycle and oil net exports using a long-term moving average of oil prices.

Table 3. Mexico: Summary Balance of Payments, 2008–2017

					Projections					
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
	(In billions of U.S. dollars)									
Current account	-17.9	-5.3	-4.8	-11.6	-11.1	-13.5	-14.7	-16.0	-15.8	-16.6
Merchandise trade balance, f.o.b.	-18.2	-5.2	-3.3	-1.7	-0.7	-3.2	-5.2	-7.1	-6.6	-5.3
Exports	291.3	229.7	298.5	349.4	375.1	396.8	419.2	446.5	477.1	514.8
Imports	-309.5	-234.9	-301.7	-351.1	-375.8	-400.0	-424.4	-453.6	-483.7	-520.1
Factor income	-18.1	-13.3	-13.0	-18.7	-19.4	-19.683	-19.4	-19.3	-19.6	-21.9
Net services	-7.1	-8.5	-10.1	-14.2	-14.4	-14.583	-15.0	-15.3	-15.6	-16.0
Net transfers	25.5	21.6	21.5	23.0	23.4	23.990	24.8	25.7	26.0	26.5
of which Remittances	25.1	21.3	21.3	22.8	23.2	23.791	24.6	25.5	25.8	26.3
Financial account	24.5	26.9	44.9	42.0	47.1	29.5	26.7	26.0	23.8	23.6
Public sector 1/	14.9	11.9	33.3	37.0	39.0	24.3	16.4	11.6	3.8	4.1
Medium- and long-term borrowing	-2.4	8.0	10.2	5.3	-1.9	-1.0	-1.0	-1.0	-1.0	-1.0
Disbursements	8.8	19.1	18.8	21.1	12.4	13.1	13.8	13.8	10.8	14.5
Amortization 2/	11.1	11.1	8.7	15.8	14.3	14.1	14.8	14.8	11.8	15.5
Pidiregas, net 3/	12.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other, including non-resident purchases of domestic bonds	4.4	4.0	23.1	31.6	40.9	25.3	17.4	12.6	4.8	5.1
Of which: oil hedging capital income	...	5.1	...	...	...	...	...	...	...	...
Private sector	9.6	15.0	11.6	5.0	8.1	5.2	10.3	14.4	20.0	19.5
Direct investment, net	26.1	7.9	4.7	9.7	13.2	12.9	14.2	14.7	15.3	15.9
Bonds and loans	-2.5	-1.5	40.2	5.4	-1.3	-3.0	0.6	2.8	7.6	6.3
Equity investments and change in assets abroad	-14.0	8.6	-33.2	-10.1	-3.8	-4.7	-4.6	-3.1	-2.9	-2.7
Errors and omissions and valuation adjustments	0.3	-16.5	-17.7	-2.5	-15.0	0.0	0.0	0.0	0.0	0.0
Net international reserves (increase -)	-7.4	-5.4	-22.8	-28.9	-21.0	-16.0	-12.0	-10.0	-8.0	-7.0
	(In percent of GDP, unless otherwise indicated)									
Memorandum items:										
Current account balance	-1.6	-0.6	-0.4	-1.0	-1.0	-1.1	-1.2	-1.2	-1.1	-1.1
Nonoil current account balance 4/	-2.9	-1.7	-1.5	-2.1	-2.0	-2.0	-1.8	-1.7	-1.4	-1.3
Nonoil trade balance 4/	-3.0	-1.8	-1.4	-1.3	-1.1	-1.1	-1.0	-1.0	-0.8	-0.5
Merchandise exports	26.4	26.0	28.8	30.2	32.3	32.8	32.9	33.4	33.8	34.6
Petroleum and derivatives exports	4.6	3.5	4.0	4.9	4.9	4.7	4.2	3.9	3.5	3.2
Merchandise imports	-28.0	-26.6	-29.1	-30.4	-32.3	-33.1	-33.4	-33.9	-34.3	-35.0
Petroleum and derivatives imports	3.2	2.3	2.9	3.7	3.9	3.8	3.6	3.4	3.2	3.0
Oil trade balance	1.4	1.2	1.1	1.2	1.0	0.8	0.6	0.5	0.3	0.2
Nonoil Exports volume growth (in percent)	0.4	-7.3	17.3	3.3	9.1	7.3	7.7	7.9	7.8	8.4
Nonoil Imports volume growth (in percent)	0.8	-22.0	24.1	8.6	7.3	7.2	7.2	7.6	7.0	7.5
Gross financing needs (billions of US$)	90.0	70.6	77.9	117.3	114.5	112.3	109.9	112.7	109.0	125.9
Gross international reserves (change, billions of US$) 5/	8.1	4.6	20.7	28.6	21.0	16.0	12.0	10.0	8.0	7.0
End-year (billions of US$)	95.3	99.9	120.6	149.2	170.2	186.2	198.2	208.2	216.2	223.2
Months of imports of goods and services	3.1	4.4	3.7	3.8	4.4	4.7	4.9	4.9	4.8	4.7
Percent of broad money	18.0	17.2	17.5	21.2	20.7	20.6	20.3	19.7	18.9	17.9
Percent of foreign portfolio liabilities	34.9	41.6	39.6	48.2	48.4	49.1	49.5	49.6	50.1	50.2
Percent of short-term debt (by residual maturity) 6/	147.0	154.9	174.0	179.7	190.9	206.5	221.8	236.5	245.5	242.4
Gross total external debt	18.6	22.0	23.9	24.3	27.4	28.1	28.1	27.8	27.1	25.7
Of which: Public external debt	11.9	13.6	15.3	16.1	19.4	20.7	20.9	20.7	19.9	18.5
Gross total external debt (billions of US$)	205.3	195.0	247.6	281.0	318.7	340.0	357.1	371.4	382.9	382.9
Of which: Public external debt 7/	131.8	120.4	158.9	186.2	225.2	249.6	266.0	277.6	281.4	274.8
External debt service (in percent of exports and other FX income) 8/	6.8	6.7	4.8	6.5	5.9	5.5	5.4	5.2	4.4	5.0

Sources: Bank of Mexico; Secretariat of Finance and Public Credit; and Fund staff projections.

1/ Including the financing of PIDIREGAS.

2/ Includes pre-payment of external debt.

3/ Break in the series in 2009 due to accounting changes.

4/ Excluding oil exports and petroleum products imports.

5/ Excludes balances under bilateral payments accounts. For 2009, includes the allocation of SDR 2.337 billion in the general allocation implemented on August 28, 2009, and another SDR 0.224 billion in the special allocation on September 9.

6/ In percent of short-term debt by residual maturity. Historical data include all prepayments.

7/ Includes gross external debt issued by the federal government, development banks and nonfinancial public enterprises. Adjusted for PIDIREGAS, and includes non-residents' holdings of domestic-currency debt.

8/ Includes amortization on medium and long-term bonds and debt, and interest payments.

Table 4. Mexico: External Financing Requirements and Sources, 2008-2014

(In billions of U.S. dollars)

	2008	2009	2010	2011	2012 Proj	2013 Proj	2013 Adv. Scenario	Contribution to Gap	2014	2014 Adv. Scenario	Contribution to Gap
Gross financing requirements (A)	**90.0**	**70.6**	**77.9**	**117.3**	**114.5**	**112.3**	**106.1**		**109.9**	**107.7**	
Current account deficit	17.3	5.1	4.5	11.1	11.1	13.5	23.3	9.8	14.7	24.5	9.8
Public sector medium and long term amortization 1/	14.4	11.1	8.7	15.8	14.3	14.1	14.1		14.8	14.8	
Public sector bonds 2/	6.9	4.9	5.5	8.2	8.1	7.9	7.9		7.7	7.7	
Public sector MLT debt	4.2	6.2	3.2	7.5	6.2	6.2	6.2		7.2	7.2	
PIDIREGAS 3/	3.2	0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Private sector medium and long term amortization 4/	14.4	14.0	13.7	23.0	25.2	25.5	25.5		25.9	25.9	
Private sector bonds 4/	7.4	6.6	7.3	10.5	13.1	13.5	13.5		13.9	13.9	
Private sector medium and long term debt 4/	7.0	7.4	6.3	12.5	12.0	12.0	12.0		12.0	12.0	
Short term financing	36.4	35.1	28.3	38.6	42.9	43.2	43.2		42.4	42.4	
Public sector 2/	9.4	7.2	2.1	2.1	9.4	9.0	9.0		9.0	9.0	
Private sector 4/ 5/	13.1	13.0	11.3	18.6	18.7	16.4	16.4		12.1	12.1	
Trade credit 6/	13.9	14.8	14.9	17.9	14.8	17.7	17.7		21.3	21.3	
Change in international reserves	7.5	5.4	22.8	28.9	21.0	16.0	0.0	-16.0	12.0	0.0	-12.0
Available financing (B)	**90.0**	**70.6**	**77.9**	**117.3**	**114.5**	**112.3**	**33.3**		**109.9**	**27.9**	
FDI, net	26.1	7.9	4.7	9.7	13.2	12.9	3.4	9.5	14.2	4.7	9.5
Public sector MLT flows 1/	30.8	22.6	42.0	52.7	53.3	38.4	7.4		31.3	-2.7	
of which:											
Public sector bonds 2/	2.2	10.7	10.4	13.5	6.2	6.4	5.4	1.0	6.7	5.7	1.0
Public sector MLT debt	6.5	8.4	8.4	7.5	6.2	6.7	6.7		7.2	7.2	
PIDIREGAS 3/	16.1	0.0	0.0	0.0	0.0	0.0	0.0		0.0	0.0	
Net change in nonresidents' holdings of peso denominated debt	6.0	3.5	23.1	31.6	40.9	25.3	-4.7	30.0	17.4	-15.6	33.0
Private sector MLT flows 4/	11.0	14.1	43.6	31.4	26.1	26.8	24.8		27.9	25.9	
Private sector bonds	4.7	8.7	16.6	20.5	14.1	14.8	12.8	2.0	15.9	13.9	2.0
Private sector MLT debt	6.2	5.5	26.9	10.9	12.0	12.0	12.0		12.0	12.0	
Short-term financing	35.7	33.9	38.6	35.6	43.6	42.4	34.4		45.3	37.3	
Public sector 2/	7.9	7.7	2.1	2.1	4.4	4.0	4.0		4.0	4.0	
Private sector 4/ 5/	13.0	11.3	18.6	18.7	21.4	17.1	17.1		15.7	15.7	
Trade credit 6/	14.8	14.9	17.9	14.8	17.7	21.3	13.3	8.0	25.6	17.6	8.0
Other flows	-13.6	-7.9	-50.9	-12.1	-21.8	-8.3	-36.8	28.5	-8.8	-37.3	28.5
of which:											
Increase in residents' portfolio and other investment assets	-9.8	-5.6	-36.2	-4.4	-6.1	-7.1	-28.1	21.0	-7.1	-28.1	21.0
Financing Gap (B-A) 7/	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**-72.8**	**72.8**		**-79.8**	**79.8**
In millions of SDRs								47.3			51.8
In percent of quota								1304			1430

Sources: Mexican authorities and IMF staff estimates.

1/ Including PIDIREGAS.

2/ On a BoP basis.

3/ Includes bonds and loans. For 2006-08, staff estimates based on the stock of debt at original maturity, estimated duration, and net financing data from the Balance of Payments. In 2009, assets from the PEMEX's Master Trust were used to pay down the stock of PIDIREGAS debt.

4/ Gross financing figures for 2006-09 are staff estimates based on data on the stock of debt by residual maturity, estimated duration, and net financing data from the Balance of Payments.

5/ Loans and money market instruments, estimates on original maturity basis.

6/ Includes accounts payable to suppliers and long-term trade credit.

7/ The adverse scenario applies independent shocks in 2013 and 2014 to generate an access envelope; thus the gaps in 2013 and 2014 should not be added together.

Table 5. Mexico: Public Sector Debt Sustainability Framework, 2007–2017
(In percent of GDP, unless otherwise indicated)

	Actual					Projections						
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Debt-stabilizing primary balance 9/
Baseline: Public sector debt 1/	37.8	43.1	44.5	42.9	43.8	**43.1**	**43.2**	**43.2**	**43.1**	**43.0**	**42.9**	**0.2**
o/w foreign-currency denominated	10.2	12.8	12.0	10.0	10.8	9.9	9.4	8.8	8.3	7.8	7.0	
Change in public sector debt	-0.5	5.3	1.4	-1.7	1.0	-0.7	0.1	0.0	-0.1	-0.1	-0.1	
Identified debt-creating flows (4+7+12)	-2.4	-0.1	7.1	0.7	0.9	-1.6	-1.0	-1.0	-0.9	-0.9	-0.8	
Primary deficit	-1.5	-1.4	3.3	2.2	1.0	0.0	-0.5	-0.7	-0.8	-0.9	-0.9	
Revenue and grants	21.4	23.0	22.3	22.2	22.1	22.8	22.9	22.9	23.2	22.7	22.3	
Primary (noninterest) expenditure	19.9	21.6	25.5	24.4	23.0	22.8	22.4	22.2	22.3	21.9	21.4	
Automatic debt dynamics 2/	-0.6	2.4	3.1	-2.0	0.0	-1.2	-0.1	0.1	0.2	0.2	0.3	
Contribution from interest rate/growth differential 3/	-0.5	-0.2	3.6	-1.4	-1.3	-1.2	-0.1	0.1	0.2	0.2	0.3	
Of which contribution from real interest rate	0.6	0.3	1.0	0.9	0.2	0.4	1.4	1.5	1.5	1.6	1.7	
Of which contribution from real GDP growth	-1.1	-0.4	2.6	-2.3	-1.5	-1.5	-1.4	-1.4	-1.3	-1.3	-1.3	
Contribution from exchange rate depreciation 4/	0.0	2.5	-0.5	-0.6	1.3	...	...	...	...	...	...	
Other identified debt-creating flows	-0.4	-1.0	0.7	0.4	0.0	-0.4	-0.4	-0.3	-0.3	-0.2	-0.2	
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other (transfers to stabilization funds: '-' indicates net inflows)	-0.4	-1.0	0.7	0.4	0.0	-0.4	-0.4	-0.3	-0.3	-0.2	-0.2	
Residual, including asset changes (2-3) 5/	1.9	5.4	-5.7	-2.3	0.1	0.8	1.0	1.0	0.9	0.8	0.7	
Public sector debt-to-revenue ratio 1/	176.8	187.6	199.7	193.2	198.5	189.2	188.6	188.7	186.2	189.4	192.3	
Gross financing need 6/	8.2	8.8	16.6	13.3	10.7	10.8	10.6	10.6	10.2	10.2	10.4	
in billions of U.S. dollars	84.8	96.7	147.0	138.0	123.7	125.4	128.3	135.3	137.0	143.7	154.0	
Scenario with key variables at their historical averages 7/						**43.1**	**43.3**	**43.4**	**43.4**	**43.4**	**43.4**	**-0.5**
Scenario with no policy change (constant primary balance) in 2012-2017						**43.1**	**43.7**	**44.4**	**45.1**	**45.9**	**46.7**	**0.2**
Key Macroeconomic and Fiscal Assumptions Underlying Baseline												
Real GDP growth (in percent)	3.2	1.2	-6.0	5.6	3.9	3.8	3.5	3.5	3.3	3.3	3.3	
Average nominal interest rate on public debt (in percent) 8/	7.5	7.2	6.2	6.3	6.2	6.4	6.5	6.7	6.9	7.1	7.2	
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	1.9	0.8	2.0	2.4	0.8	1.1	3.5	3.7	3.9	4.0	4.2	
Nominal appreciation (increase in US dollar value of local currency, in percent)	0.1	-19.7	3.7	5.7	-11.7	...	...	...	...	...	...	
Inflation rate (GDP deflator, in percent)	5.6	6.4	4.2	3.9	5.4	5.3	3.0	3.0	3.1	3.1	3.0	
Growth of real primary spending (deflated by GDP deflator, in percent)	4.3	9.4	11.4	0.8	-1.8	2.6	1.8	2.6	3.9	1.1	1.2	
Primary deficit	-1.5	-1.4	3.3	2.2	1.0	0.0	-0.5	-0.7	-0.8	-0.9	-0.9	

1/ Indicate coverage of public sector, e.g., general government or nonfinancial public sector. Also whether net or gross debt is used.
2/ Derived as $[(r - \pi(1+g) - g + \alpha\varepsilon(1+r)]/(1+g+\pi+g\pi))$ times previous period debt ratio, with r = interest rate; π = growth rate of GDP deflator; g = real GDP growth rate; α = share of foreign-currency denominated debt; and ε = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).
3/ The real interest rate contribution is derived from the denominator in footnote 2/ as $r - \pi(1+g)$ and the real growth contribution as -g.
4/ The exchange rate contribution is derived from the numerator in footnote 2/ as $\alpha\varepsilon(1+r)$.
5/ For projections, this line includes exchange rate changes.
6/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.
7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.
8/ Derived as nominal interest expenditure divided by previous period debt stock.
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Table 6. Mexico: External Debt Sustainability Framework, 2007–2017
(In percent of GDP, unless otherwise indicated)

	Actual					Projections						
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Debt-stabilizing non-interest current account 7/
Baseline: External debt	19.0	18.8	22.1	23.9	24.3	**27.4**	**28.1**	**28.0**	**27.6**	**27.1**	**25.7**	**-1.3**
Change in external debt	1.0	-0.2	3.3	1.8	0.4	3.1	0.7	-0.1	-0.3	-0.5	-1.4	
Identified external debt-creating flows (4+8+9)	-2.8	-0.9	3.2	-4.5	-2.5	-1.4	-1.2	-1.3	-1.3	-1.4	-1.3	
Current account deficit, excluding interest payments	-0.5	0.1	-0.8	-0.9	-0.6	-0.7	-0.5	-0.3	-0.3	-0.4	-0.6	
Deficit in balance of goods and services	1.6	2.2	1.5	1.3	1.4	1.3	1.4	1.6	1.6	1.5	1.4	
Exports	27.9	28.2	27.7	30.3	31.6	33.7	34.2	34.3	34.8	35.2	36.0	
Imports	29.5	30.5	29.2	31.6	33.0	34.9	35.7	35.9	36.4	36.8	37.4	
Net non-debt creating capital inflows (negative)	-2.4	-1.5	-1.8	-1.7	-1.0	-1.4	-1.4	-1.5	-1.6	-1.6	-1.6	
Automatic debt dynamics 1/	0.1	0.5	5.9	-1.9	-0.9	0.7	0.6	0.5	0.6	0.7	0.8	
Denominator: 1+g+r+gr	1.1	1.1	0.8	1.2	1.1	1.0	1.0	1.1	1.1	1.1	1.1	
Contribution from nominal interest rate	1.6	1.5	1.4	1.3	1.5	1.6	1.5	1.4	1.5	1.5	1.7	
Contribution from real GDP growth	-0.5	-0.2	1.4	-1.0	-0.8	-0.9	-0.9	-0.9	-0.9	-0.9	-0.8	
Contribution from price and exchange rate changes 2/	-0.9	-0.8	3.1	-2.2	-1.6	...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	3.8	0.7	0.1	6.4	3.0	4.5	1.9	1.2	1.0	0.9	-0.1	
External debt-to-exports ratio (in percent)	68.1	66.5	79.8	78.9	77.0	81.4	82.1	81.5	79.5	77.0	71.4	
Gross external financing need (in billions of US dollars) 4/	89.2	107.2	103.0	97.0	106.5	127.6	123.9	127.1	126.6	129.5	142.1	
in percent of GDP	8.6	9.8	11.7	9.4	9.2	11.0	10.3	10.0	9.5	9.2	9.5	
Scenario with key variables at their historical averages 5/						**27.4**	**27.6**	**27.4**	**27.1**	**26.7**	**25.3**	**-1.3**
Key Macroeconomic Assumptions Underlying Baseline												
Real GDP growth (in percent)	3.2	1.2	-6.0	5.6	3.9	3.8	3.5	3.5	3.3	3.3	3.3	
GDP deflator in US dollars (change in percent)	5.4	4.5	-14.2	11.1	7.2	-3.0	0.5	1.8	1.8	2.1	2.1	
Nominal external interest rate (in percent)	9.5	8.2	6.0	7.2	7.1	6.7	5.9	5.4	5.5	5.8	6.5	
Growth of exports (US dollar terms, in percent) 6/	8.8	6.9	-20.9	28.3	16.3	7.2	5.7	5.6	6.5	6.8	7.8	
Growth of imports (US dollar terms, in percent) 6/	9.7	9.1	-22.7	26.9	16.4	6.7	6.2	6.0	6.7	6.5	7.3	
Current account balance, excluding interest payments	0.5	-0.1	0.8	0.9	0.6	0.7	0.5	0.3	0.3	0.4	0.6	
Net non-debt creating capital inflows	2.4	1.5	1.8	1.7	1.0	1.4	1.4	1.5	1.6	1.6	1.6	

1/ Derived as $[r - g - \rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock, with r = nominal effective interest rate on external debt; ρ = change in domestic GDP deflator in US dollar terms, g = real GDP growth rate,
ε = nominal appreciation (increase in dollar value of domestic currency), and α = share of domestic-currency denominated debt in total external debt.
2/ The contribution from price and exchange rate changes is defined as $[-\rho(1+g) + \varepsilon\alpha(1+r)]/(1+g+\rho+g\rho)$ times previous period debt stock. ρ increases with an appreciating domestic currency ($\varepsilon > 0$) and rising inflation (based on GDP deflator).
3/ For projection, line includes the impact of price and exchange rate changes.
4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.
5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.
6/ Goods and non-factor services.
7/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

Table 7. Mexico: Indicators of Fund Credit 2012-2018

	Projections						
	2012	2013	2014	2015	2016	2017	2018
Stocks from prospective drawings 1/							
Fund credit in millions USD	72,824	72,824	72,824	72,824	36,412	0	...
Fund credit in millions SDR	47,292	47,292	47,292	47,292	23,646	0	...
In percent of quota	1,304.4	1,304.4	1,304.4	1,304.4	652.2	0	...
In percent of GDP	6.3	6.0	5.7	5.4	2.6	0	...
In percent of exports of goods and services	18.6	17.6	16.7	15.7	7.3	0	...
In percent of gross reserves	30.0	28.1	26.9	25.9	14.4	0	...
Flows from prospective drawings 2/							
Charges (Millions SDR)	236	1,145	1,244	1,244	1,275	379	5
Debt Service due on GRA credit (Millions SDR)	236	1,145	1,244	1,244	24,921	24,025	5
In percent of quota	6.5	31.6	34.3	34.3	687.3	663	0
In percent of GDP	0.0	0.1	0.2	0.1	2.7	2.5	...
In percent of exports of goods and services	0.1	0.4	0.4	0.4	7.7	6.9	...
In percent of gross reserves	0.5	2.4	2.6	2.6	104.8	16,575	...
Memo Item:							
Total External Debt (percent of GDP)	33.7	34.2	33.8	33.2	29.7	25.7	...

Sources: IMF Finance Department; Mexican authorities, and Fund staff estimates

1/ End of period. Assumes full drawings under the FCL approval, which implies that repayment starts in early 2016. The Mexican authorities have expressed their intention to treat the arrangement as precautionary. At a SDR/US$ rate of 0.64940 as of October 25, 2012.

2/ Based on the rate of charge as of October 25, 2012. Includes surcharges under the system currently in force and service charges.

Table 8. Mexico: Financial Soundness Indicators

(in percent)

	2008	2009	2010	2011	2012 1/
Capital Adequacy					
Regulatory capital to risk-weighted assets	15.3	16.5	16.9	15.7	15.7
Regulatory Tier 1 capital to risk-weighted assets	13.3	14.6	14.9	13.6	13.8
Capital to assets	9.2	10.7	10.4	9.9	10.1
Gross asset position in financial derivatives to capital	92.7	57.6	56.5	77.5	73.2
Gross liability position in financial derivatives to capital	100.4	59.5	55.6	79.6	71.9
Asset Quality					
Nonperforming loans to total gross loans	3.0	2.8	2.0	2.1	2.2
Provisions to Nonperforming loans	161.2	173.8	200.6	189.6	190.5
Earnings and Profitability					
Return on assets	1.4	1.5	1.8	1.5	1.8
Return on equity	14.8	15.2	16.8	15.5	18.2
Liquidity					
Liquid assets to short-term liabilities	56.1	57.7	58.2	55.3	55.7
Liquid assets to total assets	40.4	42.7	43.3	41.7	41.6
Customer deposits to total (noninterbank) loans	89.6	90.4	87.9	83.1	82.8

Sources: FSI & CNBV.

1/ As of March 2012

Table 9. Mexico: Proposed Access

	Proposed Arrangement FCL	Proposed Arrangement (Percentile)	High-Access Cases 1/ 20th	65th Percentile (Ratio)	80th	Median
Access						
In millions of SDRs	47,292	100	1,400	11,000	15,363	6,901
Average annual access (percent of quota)	652	78	171	457	703	300
Access during the first year (percent of quota)	326					
Average annual access (percent of total) 2/	652	78	300	754	1,009	560
Total access in percent of: 3/						
Actual quota	1,304	86	307	801	1,053	587
Gross domestic product	6.3	51	4.0	7.3	9.6	6.3
Gross international reserves	42.8	39	27	61	90	49
Exports of goods and nonfactor services 4/	18.6	43	11.3	31.5	39.3	21
Imports of goods and nonfactor services	17.9	47	10.0	25.6	37.5	20
Total debt stock 5/						
Of which: Public	14	56	9	16	31	12
External	26	88	7	15	22	12
Short-term 6/	109	82	21	49	103	33
M2	9	30	6	16	26	12

Source: Executive Board documents, MONA database, and Fund staff estimates.

1/ High access cases include available data at approval and on augmentation for all the requests to the Board since 1997 which involved the use of the exceptional circumstances clause or SRF resources. Exceptional access augmentations are counted as separate observations. For the purpose of measuring access as a ratio of different metrics, access includes augmentations and previously approved and drawn amounts.

2/ Correspond to quotas prior to 2008 Reform.

3/ The data used to calculate ratios is the actual value for the year prior to approval for public, external, and short-term debt, and the projection at the time of program approval for the year in which the program was approved for all other variables (projections for 2012 were used).

4/ Includes net private transfers.

5/ Refers to net debt.

6/ Refers to residual maturity.

Table 10. FCL for Mexico—Impact on GRA Finances
(In SDR millions, unless otherwise indicated)

	As of 11/01/2012
Liquidity measures	
Current Forward Commitment Capacity (FCC) 1/	251,615
Impact on FCC on approval of FCL (net)	-23,646
Prudential measures, assuming full FCL drawing	
Fund credit to Mexico	
In percent of total GRA credit outstanding 2/	33.9
In percent of current precautionary balances	497.8
Fund credit outstanding to five largest debtors	
In percent of total GRA credit outstanding, before approval	75.7
In percent of total GRA credit outstanding, upon approval of the FCL 2/	78.3
Memorandum items	
Current precautionary balances (FY 2012)	9,500
Total FCL commitments, including proposed FCL 3/	70,328
Quota of FTP members with actual and proposed FCLs, in percent of total quota of FTP members	3.1

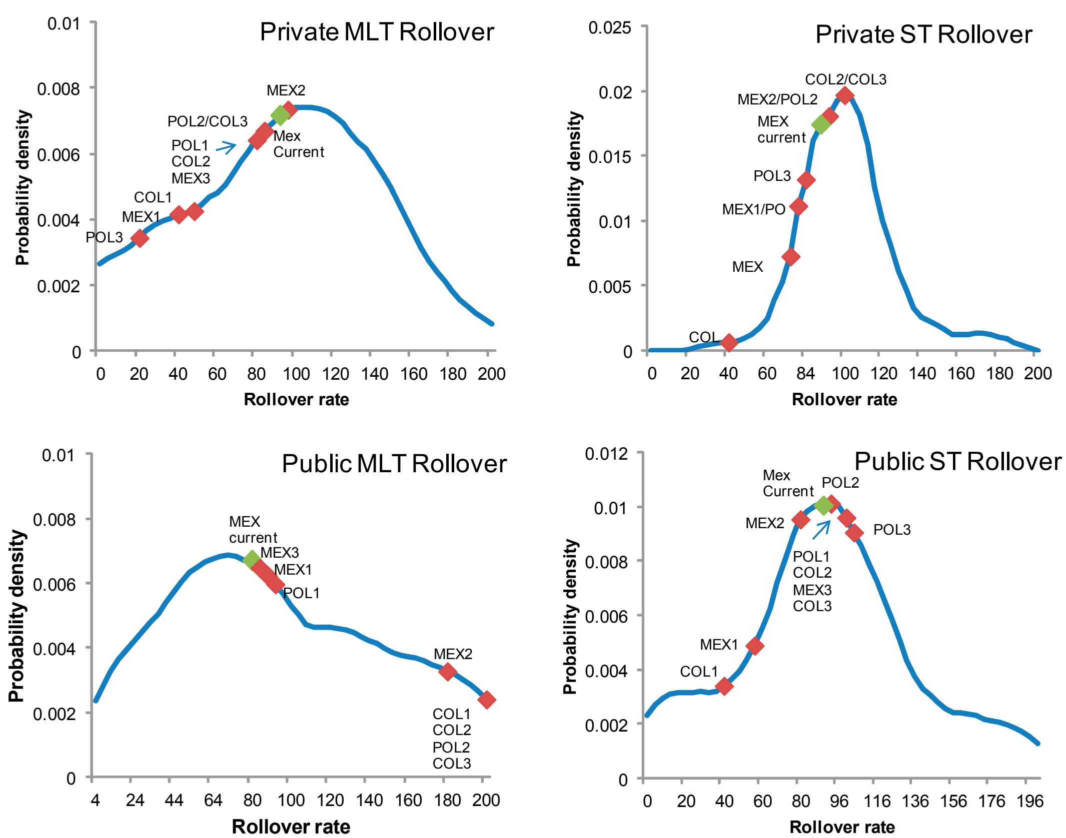
Sources: Finance Department.

1/ The FCC measures the Fund's capacity to make new credit commitments. It includes the liquidity effects of resources made available under bilateral borrowing and note purchase agreements and the NAB.
2/ Based on current Fund credit outstanding plus full drawings under the proposed FCL.
3/ Excluding Mexico's existing FCL.

Appendix 1. Rollover Rates in the Adverse Scenario

The rollover rates assumed in the adverse scenario are in line with those included in previous FCLs (Figure A1). Rollover rates for private and public sector short- and long-term debt are between 80–95 percent. They are close to the median of kernel density estimators of the distributions for the behavior of rollover rates during past exogenous stress episodes in almost 50 emerging markets.[1]

Figure A1. Empirical Adverse Shock Distributions



[1] The kernel distributions, however, do not differentiate among countries with different degrees of capital account openness.

ATTACHMENT 1

Mexico City, November 5, 2012

Ms. Christine Lagarde
Managing Director
International Monetary Fund
Washington, DC 20431

Dear Ms. Lagarde,

The current global financial conditions presented Mexico with Significant challenges, yet in spite of this, economic stability has been maintained and growth has remained resilient. As noted in the latest Article IV consultation, this has owed much to Mexico's strong policy framework, the progress made toward improving the private and public sector balance sheets over recent years, and the perception of Mexico as a prudently and well managed economy. The successive Flexible Credit Line (FCL) arrangements with the Fund have also provided important support to our macroeconomic strategy and helped sustain market confidence.

While we expect economic growth in Mexico to continue, downside risks to the global outlook have risen-as discussed in the latest World Economic Outlook and Global Financial Stability Report, and suggested by recent market indicators-increasing global uncertainty and tail risks. Against this background, we would like to request a successor 24-month FCL arrangement for Mexico for 1,304 percent of quota (SDR 47,292 million), down from 1,500 percent of quota. We believe that a new FCL arrangement, which we again intend to treat as precautionary, will continue to play a strong role in insuring against tail risk events and supporting public confidence.

Our policy priorities have continued to be to support the recovery, maintain economic and financial stability and strengthen policy buffers while building the foundations for strong and sustainable medium-term growth. On the monetary side, our policy remains underpinned by the inflation targeting regime, which has effectively anchored medium-term inflation expectations. Despite a temporary rise due to food prices in the second half of 2012, inflationary pressures have remained contained, with core inflation within the variability interval. The central bank is committed to monitor the determinants of inflation closely-including cyclical conditions, global headwinds, and the persistence of supply shocks-adjusting monetary policy as necessary to keep inflation in line with the target. The central bank win strive to communicate the stance of monetary policy vis-a-vis temporary supply shocks, in order to make clear that its primary role lies with preventing second-round effects and maintaining inflation expectations well-anchored.

Consistent with our monetary framework, we remain committed to maintaining the flexible exchange rate regime, which proved to be a key shock absorber during periods of global financial turmoil. We have continued to build our international reserves by accumulating foreign exchange receipts from Pemex and the Federal Government. The rule-based accumulation policy would allow the central bank to maintain current reserve coverage ratios, particularly those associated with balance sheet exposures that are relevant for global tail risks.

Aided by a strong regulatory framework, the banking sector remains well-capitalized with a healthy liquidity profile, and is resilient to a range of stress scenarios (as discussed in the latest report of Mexico's Financial System Stability Council and the recent FSAP Update). We have continued to take steps to improve our financial regulation and supervision, which would allow for an early adoption of most elements of the Basel III capital requirements. The National Banking and Securities Commission (CNBV) has established working groups to assess the implementation of Pillar 2 and a pilot program to address concentration risks at some banks. It has also strengthened the provisioning rules, based on expected losses, on banks' consumer loans and mortgages and on the capital requirements regime on credit to subnational governments. Furthermore, in light of the presence of foreign banks in our financial system, we continue to monitor developments closely, including through home-host supervisory colleges.

On the fiscal side, policy has remained guided by the balanced budget rule and the medium-term budgetary framework, to ensure that public debt as a share of GDP is firmly set on a downward path, providing assurances of sustainability. We have continued with the fiscal consolidation that began after the fiscal stimulus during the crisis, resulting in a significant decline in both the general and primary deficits in 2012.

With the new administration taking office in December, policy continuity is underpinned by a strong consensus in Mexico about macroeconomic stability and the current rule-based and institutional frameworks. In the context of central bank independence, monetary policy will continue to be guided by the inflation targeting framework, and the floating exchange regime will keep playing a critical buffering role. Financial oversight will continue to be based on a sound regulatory and supervisory framework. The balanced budget rule remains a key anchor for fiscal policy.

To help expand the economy's medium-term growth potential, a key developmental objective going forward, some structural reform initiatives have been advanced. During 2011, a reform to our Antitrust Law was approved and a new Public-Private Partnership Act was signed into law. Currently, proposals aimed at increasing labor market flexibility, transparency and better reporting at the subnational public sector level are being discussed in Congress.

In sum, as Executive Directors acknowledged in the latest Article IV consultation discussion, Mexico's policy framework remains very strong, and economic policies have responded in a timely and appropriate fashion in managing the impact of the global crisis and subsequently to support economic activity and rebuilding buffers. As conditions have remained similar to those observed when the previous renewal of the FCL took place, we are maintaining the same basic strategy as the one adopted then. We will continue to react as needed to any future shocks that may arise.

Sincerely yours,

/s/	/s/
José Antonio Meade Kuribreña	Agustín Guillermo Carstens Carstens
Secretary of Finance and Public Credit	Governor of Banco de Mexico

ATTACHMENT 2

Equipo de Transición
Enrique Peña Nieto
Presidente Electo de los Estados Unidos Mexicanos

Mexico City, November 5, 2012

Dear Ms. Lagarde,

On behalf of Mexico's President Elect, we fully support the current administration request for a successor 24 month FCL arrangement for Mexico. As expressed in the authorities' letter, downside risks to the global outlook have risen, increasing global uncertainty and tail risks. Against this background, an FCL arrangement for SDR 47,292 million, which we intend to treat as precautionary, will play a strong role in insuring against tail risk events and supporting public confidence.

Policy continuity is underpinned by a strong consensus in Mexico about macroeconomic stability and the current rule-based frameworks. We remain firmly committed to maintaining prudent policies within the current rules-based frameworks. This includes an independent central bank, and the floating exchange regime which will keep playing a critical buffering role. Fiscal policy will continue to be anchored by the balanced budget rule; and financial oversight will remain based on the sound regulatory and supervisory framework.

We are also convinced that it is critical to work on structural reforms in order to enhance Mexico's growth potential. The upcoming reforms and a stronger international cooperation, will present our country with the development opportunities it needs.

Sincerely yours,

/s/
Luis Videgaray Caso
Coordinador General para la Transición Gubernamental

INTERNATIONAL MONETARY FUND

Mexico—Assessment of the Impact of the Proposed Flexible Credit Line Arrangement on the Fund's Finances and Liquidity Position

Prepared by the Finance and Strategy, Policy and Review Departments
(In consultation with other Departments)

Approved by Andrew Tweedie and Lorenzo Giorgianni

November 21, 2012

1. **This note assesses the impact of the proposed Flexible Credit Line (FCL) arrangement for Mexico on the Fund's finances and liquidity position, in accordance with the policy on FCL arrangements.**[1] The proposed arrangement would cover a 24-month period and access would be in an amount of SDR 47.292 billion (1,304 percent of quota).[2] It would succeed the existing FCL arrangement of the same size in SDR terms which would be cancelled. The full amount of access proposed would be available throughout the arrangement period, in one or multiple purchases.[3] The authorities intend to treat the arrangement as precautionary.

I. Background

2. **Against the backdrop of a global economic and financial crisis, a one-year FCL arrangement equivalent to SDR 31.5 billion (1,000 percent of quota) was approved on April 17, 2009 which the authorities treated as precautionary.** This arrangement was succeeded by another FCL arrangement on identical terms approved on March 25, 2010 and a two-year FCL arrangement in the amount of SDR 47.292 billion (1,500 percent of quota) approved on January 10, 2011. Despite the sluggish U.S. recovery and persistent uncertainty from Europe, Mexico has maintained strong macroeconomic performance supported by the authorities' sound policy management, and no drawings have been made under the previous and the existing FCL arrangements.[4] As discussed in Annex I, Mexico has a history of strong

[1] See *GRA Lending Toolkit and Conditionality—Reform Proposals* (3/13/09) and *Flexible Credit Line (FCL) Arrangements,* Decision No.14283-(09/29), adopted March 24, 2009.

[2] See *Mexico—Arrangement Under the Flexible Credit Line and Cancellation of the Current Arrangement* (11/20/12). After the 2008 Quota and Voice Reform became effective, Mexico's quota increased from SDR 3152.8 million to SDR 3625.7 million.

[3] If the full amount is not drawn in the first year of the arrangement, subsequent purchases can only be made following completion of a review of Mexico's continued qualification for the FCL arrangement.

[4] Since the crisis, Mexico has benefited from the relatively good performance of the U.S. manufacturing sector (to which it is closely integrated) and achieved a strong recovery of its market share in that market.

performance under earlier Fund arrangements and an exemplary record of meeting its obligations to the Fund.

3. **Total external and public debt levels are moderate and are expected to remain stable over the medium run.** External debt increased moderately in recent years largely as a result of the depreciation of the peso, but still remains below 25 percent of GDP in 2011 and is projected to be low and sustainable over the medium term. Short-term debt on a residual maturity basis accounts for less than 28 percent of total external debt. Gross public debt is currently at about 44 percent of GDP and is projected to stabilize at around 43 percent in subsequent years. Public external debt is estimated at close to 20 percent of GDP at end 2012.[5] Sustainability analyses show both external and public debt remaining manageable under a range of scenarios, with no significant contingent liabilities incurred during the crisis.

4. **If the full amount available under the proposed FCL arrangement were disbursed in 2012:**

- Mexico's external debt would remain moderate, with Fund credit representing a significant part of this debt: total external debt would rise to about 34 percent of GDP initially, and public external debt would rise close to 26 percent of GDP, with Fund credit representing 6 percent of GDP (Table 1). Mexico's outstanding use of GRA resources would account for 19 percent of total external debt, 24 percent of public external debt, and 30 percent of gross international reserves.

- External debt service would increase in the medium-term, but remain manageable under staff's medium-term macro projections. Mexico's projected debt service to the Fund would peak in 2016 at about SDR 24.9 billion, or about 2.7 percent of GDP.[6] In terms of exports of goods and services, external debt service to the Fund would peak at about 7.7 percent, accounting for about 54 percent of total public external debt service, which would increase to just over 14 percent of exports of goods and services.

[5] For the purposes of this assessment, public external debt includes the nonresident holdings of peso-denominated debt.

[6] The figures on debt service used in this report are calculated assuming that full amount available under the arrangement is purchased upon approval of the arrangement, and that all repurchases are made as scheduled.

Table 1. Mexico: Capacity to Repay Indicators 1/

	2011	2012	2013	2014	2015	2016	2017
Exposure and Repayments (In SDR millions)							
GRA credit to Mexico	--	47,292.0	47,292.0	47,292.0	47,292.0	23,646.0	--
(In percent of quota)	--	(1,304.4)	(1,304.4)	(1,304.4)	(1,304.4)	(652.2)	--
Charges due on GRA credit 2/	--	236.5	1,144.8	1,243.9	1,243.9	1,274.7	379.1
Debt service due on GRA credit 2/	--	236.5	1,144.8	1,243.9	1,243.9	24,920.7	24,025.1
Debt and Debt Service Ratios 3/							
In percent of GDP							
Total external debt	24.3	33.7	34.2	33.8	33.2	29.7	25.7
Public external debt	16.1	25.7	26.7	26.6	26.2	22.5	18.5
GRA credit to Mexico	--	6.3	6.0	5.7	5.4	2.6	--
Total external debt service	7.3	8.4	8.5	8.2	7.9	10.3	10.2
Public external debt service	2.4	2.3	2.9	2.8	2.7	5.0	4.7
Debt service due on GRA credit	--	0.0	0.1	0.2	0.1	2.7	2.5
In percent of Gross International Reserves							
Total external debt	188.3	161.1	159.4	158.6	158.1	166.0	171.5
Public external debt	124.8	122.6	124.5	125.0	124.7	125.8	123.1
GRA credit to Mexico	--	30.0	28.1	26.9	25.9	14.4	--
In percent of Exports of Goods and Services							
Total external debt service	23.2	24.9	24.9	23.9	22.6	29.1	28.2
Public external debt service	7.5	6.9	8.5	8.2	7.8	14.2	13.1
Debt service due on GRA credit	--	0.1	0.4	0.4	0.4	7.7	6.9
In percent of Total External Debt							
GRA credit to Mexico	--	18.6	17.6	16.9	16.4	8.7	--
In percent of Public External Debt							
GRA credit to Mexico	--	24.4	22.6	21.5	20.8	11.5	--

Sources: Mexican authorities, Finance Department, World Economic Outlook, and IMF staff estimates.

1/ Assumes full drawings under the FCL upon approval. The Mexican authorities have expressed their intention to treat the arrangement as precautionary.
2/ Based on the rate of charge as of November 1, 2012. Includes surcharges under the system currently in force and service charges.
3/ Staff projections for external debt, GDP, gross international reserves, and exports of goods and services, adjusted for the impact of the assumed FCL drawing.

5. **The immediate net impact of the proposed arrangement would be to lower the Fund's forward commitment capacity (FCC) by SDR 23.6 billion (9.4 percent).** This is because:

- The current arrangement was approved before the first activation of the NAB and, under existing policies, any drawings would be financed equally by quota and bilateral resources. In the absence of a new arrangement, the cancellation of the existing arrangement would free up the quota resources (and thereby raise the FCC by SDR 23.6 billion).

- However, the freed up bilateral resources cannot be used to finance new commitments, and therefore do not lead to a corresponding increase in the FCC. While this will reduce the need to set aside NAB resources to allow for the folding in of bilateral claims, these resources cannot be used to finance new commitments unless NAB participants and the Executive Board were to approve an increase in the maximum resources available during the current activation period. Such an increase is not being proposed at this time.

- Approval of the proposed new FCL arrangement will reduce the FCC by the full amount of the arrangement. Thus, the overall net effect on the FCC is a reduction by SDR 23.6 billion (Table 2).[7]

6. **If the resources available under the proposed FCL arrangement were fully drawn, the Fund's exposure to Mexico would be large in relation to total credit outstanding and current precautionary balances:**

- Mexico would represent the Fund's largest single credit exposure at about 34 percent of total GRA credit outstanding—though this represents a reduction of 13 percent compared with the potential share at the time of approval of the current FCL.

- The concentration of Fund credit among the top five users of Fund resources would increase to about 78 percent from 76 percent currently.

- The GRA exposure to Mexico would be very large in relation to the current level of the Fund's precautionary balances. If the resources available under the arrangement were fully drawn, Fund credit to Mexico would be nearly 5 times the Fund's current precautionary balances.

[7] Staff plans to propose an amendment of the Financial Transaction Plan (FTP) and Resource Mobilization Plan (RMP) to reflect the change in the composition of potential financing under the new FCL arrangement which would be approved during the current NAB activation period.

Table 2. FCL Arrangement for Mexico—Impact on GRA Finances
(In SDR millions, unless otherwise indicated)

	As of 11/01/2012
Liquidity measures	
Current Forward Commitment Capacity (FCC) 1/	251,615
Impact on FCC on approval of FCL (net)	-23,646
Prudential measures, assuming full FCL drawing	
Fund credit to Mexico	
In percent of total GRA credit outstanding 2/	33.9
In percent of current precautionary balances	497.8
Fund credit outstanding to five largest debtors	
In percent of total GRA credit outstanding, before approval	75.7
In percent of total GRA credit outstanding, upon approval of the FCL 2/	78.3
Memorandum items	
Current precautionary balances (FY 2012)	9,500
Total FCL commitments, including proposed FCL 3/	70,328
Quota of FTP members with actual and proposed FCLs, in percent of total quota of FTP members	3.1

Sources: Finance Department.

1/ The FCC measures the Fund's capacity to make new credit commitments. It includes the liquidity effects of resources made available under bilateral borrowing and note purchase agreements and the NAB.
2/ Based on current Fund credit outstanding plus full drawings under the proposed FCL.
3/ Excluding Mexico's existing FCL.

II. ASSESSMENT

7. **The proposed FCL arrangement would have a significant but manageable impact on the Fund's liquidity position.** The current liquidity position appears sufficiently strong to accommodate the proposed arrangement, especially since the cancellation of Mexico's existing FCL would partially offset the liquidity effect from the proposed new FCL. In addition, the need to set aside NAB resources to allow for the folding in of bilateral claims would be reduced, and the 2012 bilateral borrowing and note purchase agreements will provide a further boost to the Fund's lending capacity as they become effective.[8] However, the persistent uncertainty in the global economy that could result in an increased demand for Fund resources calls for continued close monitoring of the Fund's liquidity.

8. **Mexico intends to treat the FCL arrangement as precautionary, but if drawn, this would become the Fund's largest single credit exposure**. Mexico's overall external debt and debt service ratios are expected to remain moderate even with a drawing under the arrangement. Hence, given Mexico's sustained track record of implementing very strong policies, including during the global financial crisis, and commitment to maintaining such policies in the future, Mexico's capacity to repay is projected to remain strong. Nonetheless, the scale of the Fund's potential exposure to Mexico—in conjunction with the recent increase

[8] These resources can be drawn in accordance with the borrowing modalities approved by the Board on June 15, 2012.

in lending to other members and the prospects for further credit expansion under already existing or possible new Fund arrangements—underscores the need to strengthen the Fund's precautionary balances.

ANNEX I. MEXICO: HISTORY OF IMF ARRANGEMENTS

This annex provides a brief overview of Mexico's Fund arrangements from 1983 to present.

Prior to the FCL arrangements approved in April 2009, March 2010 and January 2011, Mexico had several Fund arrangements in the 1980s and 1990s. It fully repaid its remaining outstanding credit in 2000 (Table I.1). Mexico has an exemplary track record of meeting its obligations to the Fund.

From 1983 to 2000, Mexico had two arrangements under the Extended Fund Facility (EFF) and three Stand-By Arrangements (SBAs). Below is a brief description of the two most recent SBAs:

- In February 1995, the Fund approved an SBA equivalent to SDR 12.1 billion (688 percent of quota) to support Mexico's adjustment program to deal with a major financial and economic crisis. Under that arrangement, Mexico made purchases totaling SDR 8.8 billion, and its outstanding credit peaked at SDR 10.6 billion (607 percent of quota) at end-1995 (Figure I.1). After regaining access to international capital markets in the second half of 1996, Mexico made sizable advance repurchases.

- In July 1999, an SBA equivalent to SDR 3.1 billion was approved as the recovery in economic performance was disrupted by unsettled conditions in international capital markets. Solid performance under the program supported by this SBA allowed Mexico to fully repay all its outstanding obligations to the Fund through a series of advance repurchases before the SBA expired in November 2000.

A one-year FCL arrangement equivalent to SDR 31.5 billion was approved on April 17, 2009 to support Mexico's economic policies and bolster confidence during the crisis. A successor FCL arrangement on identical terms was approved on March 25, 2010. This arrangement was cancelled and a new two-year FCL was approved in January 2011 increasing the access to SDR 47.3 billion. No drawings have been made under any of the FCL arrangements.

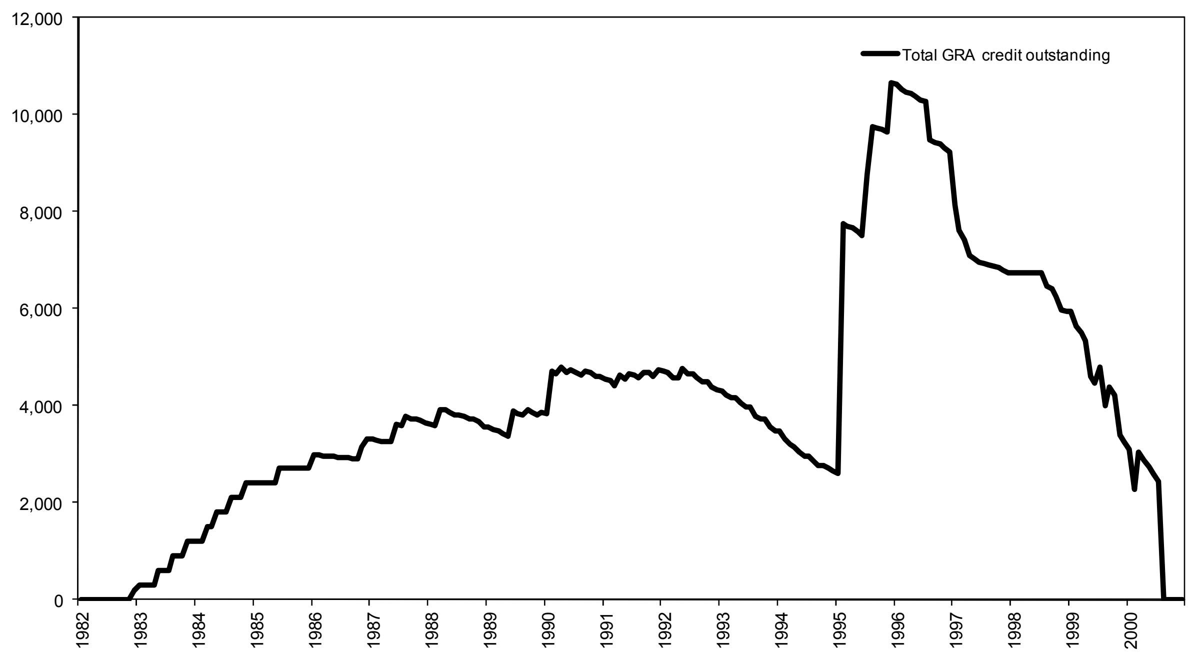
Table I.1. Mexico: IMF Financial Arrangements, 1983–2012
(In millions of SDR)

Year	Type of Arrangement	Date of Arrangement	Date of Expiration or Canellation	Amount of New Arrangement	Amount Drawn	Purchases		Repurchases	Fund Exposure 1/
1983	EFF	1-Jan-83	31-Dec-85	3,410.6	2,502.7	1,003.1		0.0	1,203.8
1984						1,203.8		0.0	2,407.5
1985						295.8		0.0	2,703.3
1986	SBA	19-Nov-86	1-Apr-88	1,400.0	1,400.0	741.4	2/	125.4	3,319.3
1987						600.0		280.0	3,639.3
1988						350.0		419.0	3,570.3
1989	EFF	26-May-89	25-May-93	3,729.6	3,263.4	943.0	3/	639.6	3,873.6
1990						1,608.4		877.1	4,604.9
1991						932.4		807.4	4,729.9
1992						233.1		636.1	4,327.0
1993						0.0		841.7	3,485.2
1994						0.0		841.0	2,644.2
1995	SBA	1-Feb-95	15-Feb-97	12,070.2	8,758.0	8,758.0		754.1	10,648.1
1996						0.0		1,413.6	9,234.5
1997						0.0		2,499.2	6,735.2
1998						0.0		783.7	5,951.5
1999	SBA	07-Jul-1999	30-Nov-2000	3,103.0	1,939.5	1,034.4		3,726.7	3,259.2
2000						905.1		4,164.3	0.0
…									
2009	FCL	17-Apr-2009	16-Apr-2010	31,528.0	0.0	0.0		0.0	0.0
2010	FCL	25-Mar-2010	09-Jan-2011	31,528.0	0.0	0.0		0.0	0.0
2011	FCL	10-Jan-2011	09-Jan-2013	47,292.0	0.0	0.0		0.0	0.0

Source: Finance Department.

1/ As of end-December.
2/ Includes a first credit tranche purchase of SDR 291.4 million.
3/ Includes a purchase of SDR 453.5 million under the Compensatory Financing Facility.

Figure I.1. Mexico: IMF Credit Outstanding, 1982–2000
(In millions of SDRs)



Source: Finance Department.

INTERNATIONAL MONETARY FUND EXTERNAL RELATIONS DEPARTMENT

Press Release No.
FOR IMMEDIATE RELEASE
November 30, 2012

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Approves New Two-Year US$73 Billion Flexible Credit Line Arrangement with Mexico

The Executive Board of the International Monetary Fund (IMF) today approved a successor two-year arrangement for Mexico under the Flexible Credit Line (FCL) in an amount equivalent to SDR 47.292 billion (about US$73 billion).[1] The Mexican authorities stated their intention to treat the arrangement as precautionary. Mexico's first FCL arrangement was approved on April 17, 2009 (see Press Release No. 09/130), and was renewed on March 25, 2010 (see Press Release No. 10/114) and January 10, 2011 (see Press Release No. 11/4).

Following the Executive Board discussion of Mexico, Mr. David Lipton, First Deputy Managing Director and Acting Chairman of the Board, made the following statement:

"Mexico has in place robust policy frameworks, which include monetary policy guided by the inflation targeting regime in the context of a flexible exchange rate, fiscal policy anchored by a balanced budget rule, and financial oversight based on a sound regulatory and supervisory framework. These frameworks have underpinned Mexico's resilience to the global crisis and strong public and private sector balance sheets. Looking ahead, the authorities remain committed to prudent macroeconomic management under these policy frameworks. They are also committed to pursuing further reforms on a variety of fronts to bolster Mexico's long-term growth potential.

"Since the global crisis, Mexico's economic growth has been resilient, supported by both external and domestic demand. Macroeconomic policies have underpinned the recovery and rebuilt policy buffers, while the exchange rate has played a key shock-absorbing role during bouts of global risk aversion. The recognition of Mexico as a prudently managed economy, with market-friendly and transparent regulations for foreign investment and open and liquid financial markets, has bolstered investor confidence and foreign portfolio investments.

[1] Amount based on the Special Drawing Right (SDR) quote of November 30, 2012 of 1 USD = SDR 0.652

"However, important risks to the global economic outlook remain, particularly from still unsettled international financial markets. Against this background, access under the Fund's Flexible Credit Line (FCL) facility has helped maintain confidence. A successor FCL arrangement with the Fund, which the authorities again intend to treat as precautionary, will continue to support the authorities' overall macroeconomic strategy, providing insurance against tail risks and bolstering market confidence," Mr. Lipton said.

The FCL was established on March 24, 2009 and further enhanced on August 30, 2010 (see Press Release Nos. 09/85 and 10/321). The FCL is available to countries with very strong fundamentals, policies, and track records of policy implementation and is particularly useful for crisis prevention purposes. FCL arrangements are approved for countries meeting pre-set qualification criteria. The FCL is a renewable credit line, which could be approved for either one or two years. Two-year arrangements involve a review of eligibility after the first year. If the country draws on the credit line, the repayment period is between three and five years. There is no cap on access to Fund resources under the FCL, and access is determined on a case-by-case basis. Qualified countries have the full amount available up-front, with no ongoing conditions. There is flexibility to either draw on the credit line at the time it is approved, or treat it as precautionary.

Mexico is a member of the IMF since 1945 and has a quota of SDR 3,625.7 million (about US$5.6 billion).