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Jan 12, 2023

R&I Affirms BBB+, Changes Outlook to Stable: United Mexican States

Rating and Investment Information, Inc. (R&I) has announced the following:

ISSUER: **United Mexican States**

Foreign Currency Issuer Rating: BBB+, Affirmed
Rating Outlook: Stable, Changed from Negative

RATIONALE:

Mexico's economy has stayed on a recovering trend. As a result of maintaining a fiscal management stance that does not rely on increased borrowing, the outstanding government debt is expected to continue to decline as a percentage of gross domestic product (GDP). The overall outlook is stable on the fiscal front, despite the outlook for a slowdown of economic growth in 2023 due to the decelerating U.S. economy and the domestic monetary tightening. There is no particular element of concern on the external front or about the country's financial system. Although attention should be paid, among other factors, to a series of government decisions to introduce policies that could discourage private companies' entry, there is a relatively smaller chance that the negative impact on the fiscal position will materialize. Based on the said recognition, R&I has affirmed the Foreign Currency Issuer Rating but changed the Rating Outlook to Stable from Negative.

Driven mainly by the robust private consumption, the economic growth in 2022 saw a firm trend, with a full-year projection at around 3%. The private investment has been supported by the trend of nearshoring, i.e. transferring a manufacturing operation to a nearby country, especially among the suppliers of automotive parts/components. However, the country's economy is expected to slow down in 2023, reflecting the stagnant exports and domestic demand due to the negative impact of monetary tightening at home and overseas along with other factors. The outlook is not optimistic, and it is highly probable that the economic growth rate of 3%, the assumption of the government budget, will not be reached.

While the current account balance is in a constant deficit, manufacturing exports and increased remittances from Mexicans abroad have curbed the scale of deficit. The country's total external debt is growing gradually but it is still under 50% as a percentage of GDP and hovering in the 30% range after adjustment of corporate debts associated with foreign direct investment. The foreign exchange reserve is abundant as a percentage to the outstanding balance of short-term debt and, on top of this, there is a Flexible Credit Line arrangement with the International Monetary Fund. The concern about the foreign exchange liquidity is limited.

A series of policy decisions in the petroleum and electricity sectors that favor state-owned enterprises for reasons such as energy security have made the private sector more dubious about the stability of the regulatory environment. Although many of them have yet to be in effect due to judicial injunctions, the direction of the current administration's economic policies is likely to act as a brake on a full-fledged investment recovery, in R&I's view. There is a concern that the improvement in the foundations for growth will be delayed, although it is an issue of high priority for the country. With regard to the government's intervention in the areas of energy etc., the governments of the U.S. and Canada have been requesting the Mexican government to come to the table in accordance with the framework of the United States-Mexico-Canada Agreement (USMCA). R&I keeps a close watch on the response of the Mexican government as well as the progress of negotiation, in light of the importance of USMCA, a trade agreement that could impact the backbone of the Mexican economy.

The government's fiscal management, which has been attentive to both supporting the economic recovery and controlling government debt is commendable. The crude oil price hikes not only led to a recovery in oil-related revenue, but also enabled the government to significantly reduce the fiscal support to Petroleos Mexicanos, a state-owned oil and gas company. Although the fiscal deficit remained slightly higher than planned in the budget, the government debt ratio has declined. The ratio is expected to

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remain stable in 2023, even though the government intends to support the economy with slightly expansive budget. There is no particular concern about the digestion of government bonds mostly by the domestic institutional investors, reflecting the decreasing share of non-residents in terms of government bond ownership.

The primary rating methodology applied to this rating is provided at "R&I's Analytical Approach to Sovereigns". The methodology is available at the web site listed below, together with other rating methodologies that are taken into consideration when assigning the rating.
https://www.r-i.co.jp/en/rating/about/rating_method.html

R&I RATINGS:

ISSUER:	**United Mexican States**
	Foreign Currency Issuer Rating
RATING:	**BBB+, Affirmed**
RATING OUTLOOK:	**Stable, Changed from Negative**

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