

MEXICAN FISCAL AND GEOPOLITICAL RISKS IN 2024

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INTRODUCTION

Macroeconomic policies, *Petroleos Mexicanos* (PEMEX) and Asian foreign investment seem to be the key drivers of the Mexican economy during 2024. The IMF, under art. IV Consultation of the IMF articles of agreement made a closed examination of the Mexican economy during 2023(IMF, 2023, pp. 1–105). The Organization pointed out the opportunities and challenges the Mexican Economy faces in 2024. Additionally, the fiscal balance of the public Mexican company PEMEX seems to represent a potential risk to the Mexican financial position due to the public company's over-indebtedness. Finally, geopolitical interest in Mexico is growing. While Asian investment is coming to Mexico due to the benefits of nearshoring and Mexican external trade policy, the United States government is worried about potential threats to national security that foreign investment in the Mexican economy could create to the U.S.

THE IMF VISIT

During the last annual International Monetary Fund visit, the Staff Report highlighted critical information for investors, policymakers, and Latin American leaders. The report highlighted that the two main risks were connected to the exchange rate and the price of oil barrels worldwide. While the exchange rate between the Mexican peso and the American Dollar has been stable, with the peso gaining territory against the dollar, the international oil price has dramatically fluctuated, causing losses in the Mexican economy.

In October 2023, the IMF Executive Board press release stipulated that Mexico should implement specific climate and financial measures to strengthen its macroeconomic position. The report recommended a switch to low carbon and renewable energy by increasing the price of carbon(IMF, 2023, p. 3). Moreover, the report suggested maintaining a high interest rate to fight inflation and reducing the interest rate only when inflation reduces consistently(IMF, 2023, p. 3). Furthermore, the staff recommended greater transparency in fiscal reporting, and policies to foster female labour force and economic empowerment(IMF, 2023, p. 3).

Mexico wants to expand its local debt while reducing its exposure to external debt in 2024. In December 2023, the Public Finance Office (*Secretaría de Hacienda y Crédito Público*) announced that their primary source for financing in 2024 was going to be the domestic market, while refinancing was also necessary to reduce the debt burden of the coming government. Moreover, the government said external debt should be reduced to decrease exchange rate risks. Accordingly, of the 48 securities listed in the Luxembourg Stock Exchange (which totalled about USD 111.888.265.000,00), only two will mature in 2024 and 2025 (LuxSE, 2024). These maturity dates will undoubtedly facilitate the external debt management strategy of the coming government as they represent bonds for £500.000.000 and USD 1.000.000.000, which are considerably lower than the total amount of the listed bonds.

PEMEX

The Fiscal Position of PEMEX is compromised, and according to senior analysts from credit ratings, its financial stability highly depends on the Mexican government's financial support. S&P (Blomberg Línea, 2023a) credit evaluation has rated PEMEX with BBB, while Moodys has rated the public company with a B1 credit rating (Blomberg Línea, 2023b). S&P has mentioned that if

the Mexican Government does not support the company, the latter would fall to a CCC+ (Blomberg Línea, 2023a). The IMF also noted the company's current debt status in its annual visit to the country.

Moreover, the transition to clean energy has a contradictory nature in Mexico. While the IMF recognized that the country depends heavily on the oil industry and pointed out the importance of improving the current status of PEMEX, they also said it was necessary to move towards clean and renewable energy sources. If the position of PEMEX does not improve, it will probably affect the Mexican government's fiscal position; therefore, the coming new president may have to address complex financial issues in the country.

Additionally, the Mexican Senate has recently approved a tax relief due to the company's fiscal pressure (BNN Bloomberg., 2023). Indirect financial assistance was crucial to the public company as PEMEX debt levels were considerably high. Just the debt listed on the Luxembourg Stock Exchange is made of 83 securities, which sum up to approximately USD 152.884.460.374 and €7.650.000.000, with almost seven bonds which sum up to approximately USD 7.749.169.000 maturing during 2024 and 2025.

Finally, PEMEX and the Mexican government have been under the spotlight due to a recent exploratory measure that, according to the Mexican government, was

necessary to guarantee hydrogen distribution in the country. The Mexican government published in the *Diario Oficial de la Federación*(Secretaría de Gobernación, 2023) a public utility declaration of the Hydrogen Plant U-3400, which is inside the *Miguel Hidalgo Refinery*, that indicated that *Pemex Transformación Industrial*, a subsidiary of *PEMEX*, had taken over the Hydron Plant. According to the media(Reuters, 2023b), this plant is owned by the French company *AirLiquide*, which expects compensation terms. Mexico and France signed (1998) and ratified (2000) a bilateral investment treaty that contained investor-state dispute resolution settlements; nonetheless, by the time of writing, no legal action against Mexico had been announced. Whether compensation comes after arbitration or conciliation, it may put additional pressure on *PEMEX*'s finances.

NEARSHORING AND ASIAN INVESTMENT

The IMF highlighted the opportunity for Mexico to nearshoring, from which Mexico already benefits. The commercial relationship between Mexico and China has strengthened recently(The New York Times, 2023). In November 2023, after the meeting between President Andrés Manuel López Obrador and Chinese President Xi Jinping, the Mexican and the Chinese governments published their intentions to articulate their commercial

strategies and cooperate to promote bilateral relations(Reuters, 2023a).

Moreover, Mexico and China have formal and informal commercial trade regulations. Although Mexico and China's commercial relations are ruled by the general norms of the World Trade Organization, they have developed a *Comprehensive Strategic Partnership* consisting of memorandums of understanding and bilateral informal working groups, reports, and recommendations. Additionally, this relationship is covered by a Bilateral Investment Agreement signed by both countries in 2008.

The development of Mexico's supply chain is noticeable, which the international media compares with other emerging economies like Thailand, Indonesia and Vietnam. Moreover, Mexico's geographical position makes it more attractive to information and technology industries as the U.S. market may need to ensure critical technological component provision, as resembled in the CHIPS and Science Act of 2022. Likewise, the Taiwanese tech company *Pegatron*(Industrial Insider, 2023) has been expanding its operation in Mexico, and the U.S. company *Cloud H.Q*(El Economista, 2023a). Moreover, goods and services arriving in Mexico can take further advantage of the United States-Mexico-Canada Agreement (USMCA), which entered into force on July 1, 2020.

Even though the U.S. and China have complex trade relations, Chinese companies still want to commercialize their products in the world's largest economy. Consequently, Chinese firms have opened branches in Mexican cities near the border, where they can move into U.S. territory. As a result, the United States has emphasized the relevance of checking current foreign investment arriving in Mexico. According to the Mexican Journal *El Economista*, Mexico and the EE.UU. have agreed to develop a mechanism that reviews foreign investment in industries such as tech, critical infrastructure, and sensitive data. According to the U.S., the arrival of external investment to Mexico and the U.S. may imply risks to the National Security. Even though the North American authorities did not point out specific countries, it is feasible that Asian investment in North America may be seen as a geopolitical risk in the region (El Economista, 2023b).

CONCLUDING REMARKS

In 2024, Mexico's public debt strategy may be highly influenced by the international oil price and dollar fluctuation. Moreover, the domestic debt market may be more active than the international bond market for Mexican securities, which may contrast with PEMEX securities, which do not have a clear path. While the Mexican government actively supports the public oil company, the latter faces financial pressures that may impact

Mexican stability. Finally, it is expected that Asian investment continue flowing into Mexican territory; however, this is without further geopolitical concern with the United States government.

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