COMPREHENSIVE GROWTH STRATEGY:

MEXICO

A. ECONOMIC OBJECTIVE AND KEY POLICY COMMITMENTS

Economic Objective

Since 2013, Mexico has pursued and enacted a historic economic reform agenda that will increase the growth potential of the economy while promoting strong, sustainable and balanced growth. Going forward, the objective of the Mexican government is to guarantee the full implementation of the reforms, mainly through the enactment of adequate secondary legislation. In particular, a number of regulatory steps are being currently implemented to ensure that the reforms become fully operational.

Key Commitments

1. Implementing the Energy Reform. Following the approval of the secondary legislation on August 7, 2014, the necessary regulations and guidelines will be issued to initiate the inflow of private investment into the sector. In addition, the government has committed $300 billion dollars to developing energy infrastructure over the next five years through the National Infrastructure Program (PNI, for its acronym in Spanish).

2. Implementing the Telecommunications Reform. The telecommunications secondary legislation was approved by Congress in June 2014. With the reform in place, the new regulator, the Federal Institute of Telecommunications, will have the faculty to promote greater competition in the sector (i.e. the definition of a dominant player in the market). This reform allows greater foreign investment in the sector and the bidding on two new national television chains, and ensures that the digital transition will be achieved by 2015.

3. Implementing the Competition Reform. In July 2014, the new Economic Competition Law became official granting new powers to the new autonomous regulator, the Federal Antitrust Commission. Using its new faculties, the Commission will enforce the antitrust legislation, that is, it will force divestment in sectors that are highly concentrated, will promote a culture of competition, and will target and prevent monopolistic practices.

4. Fostering Investment in Infrastructure through the implementation of the Financial Reform and the National Infrastructure Program (PNI). Capital market regulations will be improved and simplified to help channel more effective institutional investors and commercial banks to infrastructure projects. The private sector participation in infrastructure will also be encouraged through the National Infrastructure Fund (FONADIN) to promote Public Private Partnerships (PPP) project development. Moreover, the government has committed to channel almost $600 billion dollars to over 700 projects in energy, communications and urban development programs through the PNI over the next five years.

5. Greater financing for infrastructure and SME´s. In the next four years, the government through National Development Banks will commit almost $45 billion dollars to expanding direct and induced credit for SMEs and infrastructure.

B. ECONOMIC OUTLOOK AND CHALLENGES TO GROWTH

Current and Future Growth Prospects

Structural reforms will have a positive impact on the potential growth of the economy by increasing productivity, investment and competition. In the short term, this will help close the output gap. In the medium term, it will spur job creation, while increasing Mexico's growth potential.

	Key Indicators					
	2013* **	**2014**	**2015**	**2016**	**2017**	**2018**
Real GDP (% yoy)	1.4	2.7	3.7	4.9	5.2	5.2
Inflation (%, yoy)	3.97	4.02^	3.0	3.0	3.0	3.0
Fiscal Balance (% of GDP)**	-0.4	-1.5	-1.0	-0.5	0.0	0.0
Current Account Balance (% of GDP)	-2.1	-1.9	-2.0	-2.0	-2.1	-2.1

***A positive (negative) gap indicates an economy above (below) its potential.**
****A positive (negative) balance indicates a fiscal surplus (deficit).**
***** Indicators can be presented on a fiscal year basis, should they be unavailable for the calendar year.**
^ Source: Forecast based on Banco de Mexico's market survey among private sector analysts. Data from the October 2014 survey.

Key Drivers

In the short term, external sector demand proves to be one of the key drivers for economic growth of the country. The firm recovery in advanced economies will support export activity and, in turn, manufacturing. Likewise, public expenditure is already helping boost economic activity.

In the medium term, the aforementioned key reforms along with other reforms also recently implemented, will positively affect investment levels. Particularly, the enacted reform agenda will improve investment climate through better regulation that provides, among other benefits, legal certainty to private investment in the energy, telecommunications and financial sectors. Growth composition should change gradually and systematically insofar as the reforms are implemented.

Assessment of Obstacles and Challenges to Growth

Economic growth could be challenged by both, external and domestic factors. As far as external factors are concerned, Mexico is one of the economies most financially connected to global markets. If global economic activity remains subdued, especially in advanced economies, export dynamics in Mexico could slow down, affecting production levels, in particular in manufacturing.

As regards domestic factors, a handful of elements have limited the country's potential. In particular, productivity growth has been a binding constraint on economic growth. From 1990 to 2011, total factor productivity decreased at an annual rate of 0.4 percent. Likewise, the labor market slack has hindered growth, influenced by high levels of informal employment and low levels of competition in strategic input markets. Moreover, further progress is required in order to increase domestic demand, notably private consumption. Therefore, these and other obstacles to growth are addressed by the reform agenda adopted in 2013. The Government is working in order to rapidly implement the structural changes embedded in the reforms, for their benefits to be tangible in the near term.

C. POLICY RESPONSES TO LIFT GROWTH

New Macroeconomic Policy Responses (including Reforms to Frameworks)

The Fiscal Reform approved in 2013 and implemented in 2014 broadens the tax base and limits special treatments, while promoting a simpler and progressive tax code. The approved measures modify all components of the tax system. As a fiscal policy measure, the reform promotes job formality with the establishment of a new tax incorporation regime. Furthermore, as mentioned above, the reform includes a Structural Balance Rule, adding a maximum limit of current expenditure growth so as to generate savings and to guarantee a higher quality in public spending.

Fiscal Reform

Regarding corporate taxation, the repeal of the Single Rate Business Tax Law or flat tax (IETU), as well as the Cash Deposit Tax Law (IDE) have been approved, simplifying the corporate tax regime. The new Income Tax Law (ISR) eliminates or limits several special regimes, including the simplified and fiscal consolidation regimes so tax evasion and deductions are limited; at the same time, it broadens the tax base in order to substitute the tax collection associated with the two taxes that were abolished. This will simplify the system, replacing the three former taxes with only one tax, while maintaining revenue collection levels. Thus, the administrative burden associated with paying taxes is reduced and the collecting efficiency is increased.

Regarding the personal income tax, the measures proposed to broaden the tax base and strengthen its progressivity were approved. A new schedule was approved for the Income Tax for individuals, including new segments and an increase to the marginal rate for high-income individuals, reaching 35% for individuals with an annual income above Ps. 3 million.

Likewise, a global limit was passed on personal deductions equivalent to 4 minimum wages or 10% of income. Furthermore, this global limit will not apply to donations by individuals or to the payment of school tuition. Moreover, the taxation of capital gains and dividends from the Mexican Stock Exchange was approved.

Regarding VAT, proposals were approved regarding the equalization of VAT in the border region to the rate prevailing in the rest of the country, as well as the preservation of the zero rate on food and medicine and the elimination of the exemption for temporary imports.

Regarding excise taxes, the approval of a special tax (IEPS) on flavored drinks was complemented by the tax set on non-basic high-calorie density foods at a rate of 8%. Furthermore, it was established that tax collection proceedings from the IEPS on flavored drinks would be used for public health programs.

Regarding green taxes, the IEPS on carbon was approved, introducing a limit of 3% tax on the price of fuel and the specification that natural gas will represent the zero-based with regard to emissions. Consistent with the extra-fiscal purpose of this tax, its payment through carbon credits is also allowed. Similarly, the tax on pesticides was approved starting in 2014.

With respect to mining, the proposed royalty was approved with amendments that allow certain credits and an exemption for small mining producers, as well as an increase in the resources destined for local governments. A new schedule for the update of water royalties was also approved.

The changes to the Fiscal Code of the Federation are aimed at facilitating compliance with fiscal obligations, strengthening the mechanism of exercising taxpayer rights and granting greater rights to the authority to combat tax fraud.

To facilitate tax compliance, the registration in the Federal Taxpayer Registry (RFC) is simplified, that is, it can be done online and though different electronic media. The Tax Mailbox has been created in order to modernize communication between taxpayers and tax authorities.

Taxpayer rights are strengthened by forcing the tax authority to inform on the advances of audits to firms' boards, establishing a new mediation mechanism between taxpayer and tax authority, regulating the embargo on bank accounts and establishing a limit on the deferral of the prescription of fiscal credits. In addition, authority is allowed to leave without effect fiscal receipts issued for non-existent operations and deadlines for debt collection procedures are reduced.

Fiscal Framework Reform

In December 2013, Congress approved the reform of the Federal Budget and Fiscal Responsibility Law. The reform strengthens macroeconomic stability, grants credibility and transparency to the evolution of expenditure and public finances in Mexico, and establishes fiscal discipline as a State Policy.

The reform strengthens the current budget balance rule, by adding a current expenditure cap. This cap ensures a return to a balanced budget in the medium term and assures an improvement in spending quality. Hence, fiscal policy will be more counter-cyclical than it has been in the past.

Second, Public Sector Borrowing Requirements (PSBR) are established as a fiscal anchor that guarantees a sound management of public finances in the medium term. This measure is broader than the current definition of traditional balance and, therefore, will provide greater transparency to the efforts of maintaining public debt in a sustainable path.

Although originally proposed as part of the fiscal reform, a simplification of the mechanism of distribution and savings of excess revenues was included in the secondary legislation of the Energy Reform (see Other Measures for further details of the Energy Reform), as well as the creation of the Mexican Oil Fund for Stabilization and Development.

- **Stabilization Funds.** The Reform increased the limits of stabilization funds so that the Federal Government and the Mexican States have greater margin to respond to adverse shocks. This increment will provide more resources to accumulate and reach a level that allows a response to a negative shock in income, as the one experienced during the 2009 crisis and that represents an extreme case of the shocks to which public finances are exposed. In order to harmonize the management of surplus revenues, the stabilization funds will become the first mechanism to cover public finances' contingencies so that the long-term savings in the Mexican Oil Fund are used only in extraordinary cases in which public finances face severe shocks that could last for over one fiscal year.
- **Mexican Oil Fund for Stabilization and Development.** The Mexican Oil Fund for Stabilization and Development, which is a savings fund that concentrates all the revenues from the energy sector, has been created. The Fund will allocate an amount equivalent to 4.7 percent of GDP of oil revenues to the Expenditure Budget, which is the amount that it currently received. Resources above this threshold would go into a long-term savings fund. Once the savings in the fund reach a threshold of 3 percent of GDP, the government would be able to make use of 60 percent of the excess resources. The Technical Committee of the Fund shall consist of three members of the Sate: the Minister of Finance, who will be chair of the committee and has a casting vote, the Minister of Energy and the Governor of the Central Bank of Mexico, as well as four independent members, appointed by the President with the Senate approval.

Monetary Policy

The Central Bank of Mexico's constitutional mandate is to pursue stability of the purchasing power of the national currency. To meet this objective, Banco de Mexico adopted an inflation-targeting scheme as framework for the monetary policy conduct. Specifically and consistent with its mandate, the Central Bank has defined as a permanent target reaching an annual inflation of 3 percent in an efficient way, that is, at the lowest possible cost to society in terms of economic activity. The conduction of monetary policy in Mexico under an inflation-targeting scheme has contributed to anchor inflation expectations, reducing the level, volatility and persistence of inflation.

Exchange Rate Policy

In Mexico, the Foreign Exchange Commission (composed by the Ministry of Finance and the Central Bank) is responsible for conducting the foreign exchange policy. The flexible exchange rate regime in Mexico has served as a natural shock buffer to attenuate the impact of adverse external events. Various elements have strengthened the role of the exchange rate as a buffer against the referred shocks. First, there has been a reduction in recent years in the pass-through of exchange rate fluctuations to domestic prices. Second, the existence of a well-developed derivatives market in Mexico, which allows economic agents to cover their exchange rate risks. Hence, due to its stabilizing properties, the flexible exchange rate regime will remain an important element of the policy framework in Mexico.

New Structural Policy Responses

Investment and Infrastructure

Mexico has enacted an ample reform agenda that will increase the growth potential of the economy. On the economic front, the most important ones are: Labor Reform, Education Reform, Telecom Reform, Anti-trust Reform, Fiscal Reform, Financial Reform and Energy Reform. The enacted reform agenda aims at the supply side of the economy, and will improve significantly the investment climate and the intermediation process of Mexico, enhancing the country's attractiveness for investment and contributing to close the gap between long-term financing needs and capital availability.

- In order to attract investment in high quality infrastructure projects and Small and Medium Enterprises (SMEs), one of the most important domestic challenges is related to the efficient implementation of these reforms.
- The role of National Development Banks is strengthened regarding infrastructure and SME financing.

Mexico's Federal Government recently presented the National Infrastructure Program 2014-2018, which includes a comprehensive infrastructure development strategy that aims to increase the country's economic growth and productivity. Mexico has several public and private sector financial vehicles to promote investment in infrastructure, as well as a recently revised legal framework that fosters private participation. Nonetheless, some challenges prevail regarding infrastructure development and financing:

- Institutional investor's participation in infrastructure is limited due to the lack of appropriate financing vehicles and infrastructure investment and risk management expertise. Also, current incentives among institutional investors account for a low risk appetite for infrastructure products.
- Despite there being a wide range of infrastructure projects in different stages of structuring, it is necessary to consolidate a pipeline of bankable projects that meet the national strategy for infrastructure development.

Employment

The comprehensive structural reform agenda that Mexico has undertaken will produce a definite impact on employment. This increase will result from greater economic growth and a more efficient labor market.

One of the challenges Mexico is facing is developing a labor market that is flexible and inclusive, that is conducive to higher labor productivity and increases real wages, promoting higher growth rates for the country. In November 2012, a Comprehensive Labor Reform in Mexico was approved by Congress. The reform is expected to contribute to a more flexible labor market, promote formal employment and increase labor productivity.

The said reform addresses many of the country's employment gaps. Regarding flexibility, it allows firms to have training programs, trial contracts and temporary contracts for specific activities. It also sets a cap on back wages in order to reduce market frictions and increases efficiency and transparency in labor unions. Moreover, it protects vulnerable groups, especially women and the disabled, while reinforcing health and civil protection measures.

In the Inflation Report, October-December 2012, Banco de Mexico quantifies the expected impact that the Labor Reform would have on output. According to this estimate, the impact on the potential GDP growth rate over the next five years could be an average of 0.15 percentage points per year. This scenario is considered the most probable, while a more optimistic scenario would increment the potential GDP rate by an average of 0.25 percentage points per year.

As part of the fiscal reform approved in 2013, several measures were included to foster formality. The proposal for a Regime of Incorporation, which substitutes the Intermediate Regime and the Regime for Small Taxpayers, was approved. The new regime provides an entry point to formality for small and medium enterprises, allowing them to be completely incorporated to the general regime after 10 years. Individuals with annual incomes of up to Ps. 2 million are allowed to pay taxes under this regime.

Additionally, the government proposed the introduction of an Unemployment Insurance Facility for formal workers. However, this measure still requires approval by Congress. The said program creates adequate conditions for a successful reintegration of the worker into the labor force, promoting labor market efficiency. The benefits include an appropriate job search that matches worker's abilities and aspirations with those of firms in case of unemployment. It encourages the creation of formal jobs by maintaining the current costs of social security for employers. The reform is expected to positively impact productivity. In the absence of household income, workers might accept less productive jobs than those they could accept if they had an income that would allow them to keep searching for an opportunity that better matches their skills and qualifications. The design of the Unemployment Insurance ensures stability of public finances.

Finally, on September 8, 2014, the Mexican Government introduced a new strategy that seeks to provide incentives for the millions of workers to join the formal economy. As part of the Fiscal Reform, *"Crezcamos Juntos*" is a program that involves various areas and levels of the government, as well as the private sector. In order to make the transition from informality to formality attractive, the program involves various incentives such as social benefits, while offering a smooth transition for those involved.

Competition

Last year, Mexico enacted a series of reforms that tackle, directly or indirectly, the lack of competition in strategic markets. In this matter, Congress approved a constitutional Anti-trust Reform, which among other factors, gives the Federal Antitrust Commission (COFECE) more autonomy and legal authority to regulate the access to essential inputs.

To implement the constitutional reform, on April 30, 2014, the Mexican Congress passed the new Economic Competition Law.

The most important changes include:

- **New faculties of the Federal Antitrust Commission.** It grants the commission new faculties, such as declaring and regulating essential inputs, determining and establishing measures to remove barriers to entry, and compelling the divestiture of assets.

- **Monopolistic practices and market concentration.** The law adds new categories of absolute monopolistic practices and new regulatory measures to prevent and investigate market concentration.
- **Special procedures and sanctions.** The law includes various new special procedures, like initiating investigations ex officio and is accompanied by a modification to the Federal Criminal Code to include penalties for monopolistic practices.

The Financial Sector Reform will make credit more readily available and at lower cost through greater competition. Mexico already boasts one of the most open financial systems in the world. So, most financial institutions in Mexico have some form of foreign participation, if not outright ownership.

In the media and fixed-line telecommunication sector, the Telecom Reform, enacted in June 2013, aims to ensure access to information technology and telecommunication and broadcasting services, including broadband.

A key measure introduced in the secondary legislation in 2014 is the definition of a dominant player, which designates an entity which amounts to more than 50% of the market share in a specific part of the telecoms or broadcasting sector. The law also establishes tighter regulation for any dominant players, including outlawing interconnection fees and forcing firms to share infrastructure. While the new regulation does impose conditions on the television sector, an important impact will be felt immediately in the telephone sector. One way the Reform seeks to attract new competitors into the TV market is by bidding for two new national chains.

Furthermore, the government continues to promote foreign direct investment. Thus, under the Telecom Reform, greater foreign investment in the sector is allowed. In the case of telecommunications, foreign investment can represent up to 100% of total investment (it was previously limited to 49%). In turn, this will increase the penetration of fixed telephone lines, mobile telephony, internet and broadband, and bring them to the levels observed in other developed countries. The government has also committed 100 billion to developing communications infrastructure through 2018.

Additionally, the Energy Reform opens up investment in the nation's energy sector to private sector participation. With this reform, the government will be able to perform exploration and extraction activities of oil and other hydrocarbons through contracts with PEMEX and/or the private sector. Moreover, PEMEX and CFE will have more technical, managerial and budgetary autonomy, which will contribute to a more competitive provision of services.

Trade

Over the last 20 years, Mexico has taken important steps to strengthen and promote the free flow of goods, services and financial resources. The country boasts free-trade agreements with over 40 countries, including nearly all G20 members, and continues to pursue the strengthening of its trade links.

Mexico has been actively working in the construction of the Trans-Pacific Partnership (TPP), which seeks to establish a free trade area in the Asia-Pacific region. Furthermore, the TPP aims to be more ambitious than a traditional free trade agreement, as it seeks to eliminate or reduce all barriers to trade, and boost investment substantially between the participating economies, which represent nearly 40% of world GDP.

The country has also been working on obtaining the benefits of its large and growing infrastructure, as well as its strategic geographical position. To assist merchandise border crossing with the United States, both governments agreed to launch a Cross-Border Long-Haul Trucking Pilot Program, so that carriers from the US and Mexico can engage in cross-border trucking operations into the other country. This program is still in its early stages, but it is a step forward to increase efficiency, and decrease transportation and environmental costs.

The structural reform agenda approved last year will have a key impact on the Mexican external sector, including trade. Broadly, these reforms seek to reduce barriers to foreign direct investment, relax equity restrictions in transport, media and fixed-line telecommunications, as well as in financial services. Moreover, they facilitate entrepreneurship and business start-ups and reduce barriers to entry and competition in strategic input markets, while relaxing constraints against private investment in the energy sector.

Other Measures

Energy Reform

On December 12, 2013, a historic Constitutional Energy Reform was approved by Congress. The reform opens investment in the nation’s oil sector to private companies. This will have a sizable positive impact on economic growth. It will also allow Mexico to tap into its vast natural gas reserves. Together with efficiency gains in the economy from lower energy prices, the reform is expected to increase potential output by 1 percent of GDP by 2018.

On August 11, 2014, President Peña Nieto signed into law the secondary legislation of this Reform and announced 10 measures to guarantee its full and efficient implementation. Among them were publishing the results of the “Round Zero”, that is, the fields awarded exclusively to PEMEX for exploration and drilling, and announcing the fields that will be open to private investment (“Round One”). Other actions included the establishment of the new energy regulatory bodies: the National Agency of Industrial Safety and Environmental Protection, the National Energy Control Center (CENACE) and the National Center for Control of Natural Gas (CENAGAS). Additionally, several programs were established to encourage the formation of human capital in the sector, to strengthen the Mexican Petroleum Institute, which conducts research and development, and to foster the use of renewable energy. With this reform, the Mexican Government will be able to perform oil and other hydrocarbons exploration and extraction activities through contracts with PEMEX and/or the private sector. The contracts include: services, profit-sharing, production-sharing, licenses or any combination of the aforementioned options. The National Hydrocarbon Commission (CNH, after its name in Spanish) will be in charge of the bidding processes and management of such contracts. Oil companies will have the right to book expected benefits of contracts in their balance sheets. However, they must specify that hydrocarbons are owned by the Mexican State.

The reform also creates the Mexican Oil Fund for Stabilization and Development. The Fund will receive and manage oil revenues in order to promote sound public finances in Mexico. Moreover, the Fund will channel resources for long-term savings, the universal pension system, science and technology, infrastructure for development, scholarships, among others.

Private investment in oil refining and processing will be allowed, as well as in oil transportation, storage and the distribution of natural gas, gasoline, diesel and other oil derivatives. In addition, the private sector will be able to participate in all the petrochemical chain and to perform activities of generation and commercialization of electricity. Transmission and distribution of electricity by the private sector will be done under contracts with the Federal Electricity Commission (CFE, after its name in Spanish).

The CNH and the Energy Regulatory Commission (CRE, after its name in Spanish) will be strengthened with the reform. Both commissions will be constituted as regulatory coordinated organisms, with their own legal personality, technical, managerial and budgetary autonomy. Commissioners will be proposed by the Executive branch of the government and confirmed by the Senate. Furthermore, PEMEX and CFE will have more technical, managerial and budgetary autonomy.

CENAGAS will be a public entity in charge of managing the pipelines and storage system, while CENACE will be removed from CFE and transformed into a public entity in charge of the national electricity system operation.

The State will protect and take care of the environment through strict sustainability criteria, promoting cleaner energy and fuels, as well as stimulating the reduction of pollutant emissions from the energy industry. The reform creates a decentralized agency for the regulation and supervision of industrial security and environment protection in the hydrocarbon sector.

Within the mining industry, the reform keeps the possibility of exploiting gas associated with carbon mining.

Secondary Legislation

On August 7, 2014, Mexico Upper House approved the complete secondary legislation for the Energy Reform. This new legal framework establishes free competition between state enterprises and private individuals in all energy activities. Additionally, it strengthens public companies and regulators (Energy Regulatory Commission and the National Hydrocarbons Commission) and the Ministry of Energy.

The secondary legislation approval includes the following five main themes:

1. **Exploration and Extraction Contracts**.
    a. The auction process for exploration and extraction contracts will be managed by the CNH, and any firm can participate. However, the Ministry of Energy (SENER) will determine which fields are up for auction and the form of contracting (profit sharing, service contracts, production sharing or licenses). Lastly, the Ministry of Finance (SHCP) will determine the economic terms of the contract.
2. **Energy Policy and Regulatory Bodies**.
    a. The National Gas Pipeline Center (CENAGAS) will be in charge of operating and overseeing the national network of hydrocarbon transportation pipelines and storage facilities system.
    b. The Electric Energy National Control Center (CENACE) will be in charge of managing the National Electric System and operating the electric wholesale market.
    c. Legislators approved that by January 1, 2016 private firms will be able to set up gas stations without them being a PEMEX franchise, however PEMEX will be their sole supplier. Furthermore, by January 1, 2017, firms will be allowed to self-supply gas. Private participation in gas distribution will enable more job creation.
    d. Additionally, from 2015 to 2017, SHCP will determine gasoline prices based on inflation and international prices. Beginning from 2018, gasoline prices will be liberalized.
3. **Regulation for Production Companies**.
    a. The body of State Productive Companies (SPC) is created with managerial autonomy and regulated independent bodies. This way, SPCs' main goal will be to maximize economic gains for the state, with a structure more similar to a private company.
    b. As an anticorruption measure, SPCs must have complete information systems regarding their suppliers and contractors, which will have to be updated on a regular basis.
    c. Pemex and CFE as SPCs will be subject to an annual evaluation, which will be carried out by a Commissioner that will have to be an independent expert.
4. **Opening of the Domestic Energy Market**.
    a. CFE will remain an electric service provider for residential consumers and for small medium commercial & industrial clients. These users will not see changes in the way they currently pay or consume electricity.
    b. Electric plants, except those intended for self-supply or of smaller than 0.5MW capacity, will require a permission from the Energy Regulatory Commission to generate electricity.

5. **Tax Regime.**

   a. PEMEX and CFE will be required to annually submit to SHCP their annual report on earnings and prospects. SHCP will determine the dividend to be paid by PEMEX and each of its productive subsidiaries.

It is plausible that, in preparation for this, enterprises may start (or perhaps have done so already) to invest immediately (in facilities, equipment, among others), which would boost jobs in the short term. Additionally, we expect to see an increase in potential growth in the long run and a gradual decline in energy prices.

Law to Increase Productivity and Competition

In October 2014, the current Administration presented the Law to Increase Productivity and Competition in the Economy. The law seeks to bolster the integration of production chains (SMEs with large enterprises), to increase the added value of exports, to strengthen the domestic market, to bolster financing activities and projects that have productive potential, as well as to increase investment in human capital, entrepreneurship and applied innovation.

ANNEX 1: ST. PETERSBURG FISCAL TEMPLATE — UPDATE

1. Update on Fiscal Strategy:

Mexico's fiscal strategy for the 2014-2018 period aims at securing a downward trend of public debt through a comprehensive fiscal consolidation strategy that includes a fiscal reform, the strengthening of the Fiscal Responsibility Law, and mechanisms to contain current expenditure and to improve the efficiency and quality of public spending in infrastructure, health and poverty alleviation programs. We expect the ratio of public debt to GDP to peak in 2015-2016 and follow a downward path thereafter.

2. Medium-term projections, and changes since last submission (required for all members):

		Estimate	Projections				
	2013*	2014	2015	2016	2017	2018	2019
Deficit[1]	2.3	3.5	3.5	3.0	2.5	2.0	2.0
ppt change	0.3	1.7	1.6	1.1	0.7		

* Figures can be presented on a fiscal year basis, should they be unavailable for the calendar year.
1/ Includes Pemex investment.

Economic assumptions, and changes since last submission (required for all members):

The debt-to-GDP ratio and deficit projections are contingent on the following assumptions for inflation and growth:

		Estimate	Projections				
	2013*	2014	2015	2016	2017	2018	2019
Real GDP growth	1.4	2.7	3.7	4.9	5.2	5.2	5.2
ppt change	-1.7	-1.3	-0.3	0.9	1.2		
ST interest rate[1]	3.8	3.0	3.3	3.9	4.5	5.0	5.5
ppt change	-0.3	-1	-1.7	-1.2	-0.9		

* Figures can be presented on a fiscal year basis, should they be unavailable for the calendar year.
1/ Average short-term interest rate (Cetes 28 days).

ANNEX 2: NEW POLICY COMMITMENTS

Macroeconomic Policy Responses (including Reforms to Frameworks)

1. Investment and Infrastructure

The new policy action:	**1. Execute the National Infrastructure Program 2014-2018 in order to promote domestic demand, job creation and lead to productivity increases.**
Implementation path and expected date of implementation	• The Federal Government recently presented the National Infrastructure Program 2014-2018 (NIP), which includes a comprehensive infrastructure development strategy that aims to increase the country's economic growth and productivity, based on three guiding principles: 1) Logistics Platform 2) Balanced Regional Development 3) Sustainable Urban Development The NIP is a broad and profound agenda for infrastructure development; it comprises 24 strategies, 83 action lines and 20 indicators with specific targets that will allow evaluating the performance of the Program. The NIP estimates a total amount of public and private investment in infrastructure to be almost \$600 billion dollars for the next five years. The Program includes 743 infrastructure projects to be developed between 2014 and 2018, in the following sectors: Energy (with investments of \$301.2 billion dollars), Housing (\$143.8 billion dollars), Communications and Transportation (\$102 billion dollars), Water (\$32.2 billion dollars), Tourism (\$14 billion dollars), and Health (\$5.6 billion dollars). This program, together with the structural reform agenda will lead to an increase in the economic growth rate of between 1.8 and 2 percentage points, and will create 350,000 additional jobs per year, reaching a total of over 1 million jobs per year. Private resources are essential to achieve the coverage and quality of the National Infrastructure Program. It is expected that the \$377 billion dollars of public investment will be complemented with \$221 billion dollars of private investment.
What indicator(s) will be used to measure progress?	Number of projects developed. Annual public and private investment in infrastructure.
Explanation of additionality (where relevant)	For more detailed information about the Program, sectors and projects please refer to http://presidencia.gob.mx/pni/

The new policy action:	2. Strengthen the role of National Development Banks for infrastructure and SME financing
Implementation path and expected date of implementation	The Financial Reform, which amended 34 laws, will enhance credit allocation in an already stable and well-capitalized financial system. Its main objective is to reduce costs and promote efficiencies in credit origination mainly for SMEs, as well as to provide a new mandate for Development Banks, in order to foster financial market development and financial inclusion. In this sense, the major National Development Banks recently presented their medium-term plans (2014-2018), which define objectives and strategies to complement commercial banks' lending, with adequate risk sharing. This will allow an increase in credit growth, in particular in areas that are not fully covered by commercial banks like infrastructure and SMEs. The main strategies include: • Expanding direct and induced credit (almost 45 billion dollars by 2018) • Fostering participation of commercial banks in infrastructure financing (mini-perm financing, mezzanine products) • Contributing to channel institutional investors' resources to infrastructure (guarantees) • Fostering infrastructure development by local governments • Strengthening credit and guarantee programs for SMEs, which will contribute to create a credit history record for these enterprises The full implementation of these strategies is fundamental for strengthening the role of National Development Banks for infrastructure and SME financing. Development Banks play an important role in complementing efforts of commercial banks to increase the supply of credit, which could serve as a catalyst for job creation and growth. During 2014, major National Development Banks' boards will take the necessary actions for the implementation of the medium-term plans.
What indicator(s) will be used to measure progress?	Balance of National Development Bank's credit as a percentage of the Gross Domestic Product (GDP).
Explanation of additionality (where relevant)	This new commitment contributes to the particular objective of the Financial Reform of providing greater flexibility to the operations of Development Banks, in order to allow them to complement commercial banks and increase credit growth, primarily in areas that influence national development.

<table>
<tr><th>The new policy action:</th><th>3. Foster private sector participation in infrastructure</th></tr>
<tr><td>Implementation path and expected date of implementation</td><td>
The Pension Funds (AFORES) are able to invest in infrastructure projects through structured instruments called Development Capital Certificates (CKDs), which are traded on the Mexican Stock Exchange. Nonetheless, a more active involvement of local institutional investors is required to fully develop local capital markets and channel more resources into long-term project financing.
In this sense, the Mexican Federal Government is encouraging a reform of capital market regulation, regarding the participation of institutional investors in infrastructure, in order to:

Improve incentives for investment portfolio management, leading to better investments and more efficient asset managers
Simplify the regulatory framework for infrastructure products, making CKDs a more flexible instrument
Extend the range of institutional investors that can invest in CKDs, including insurance companies

This policy will contribute to strengthen local institutional investors' participation in infrastructure, fostering private capital mobilization for this sector. This reform is being analyzed and will be presented during 2014.
In addition, the Federal Government has developed the National Infrastructure Fund (FONADIN), which is a specialized project-financing vehicle that promotes infrastructure development through PPP schemes.
FONADIN is the concessionaire of a network of 51 toll highways. Toll income allows financing new infrastructure projects with high social returns (using brownfield projects to finance greenfield). It is a flexible risk-taking entity that can efficiently promote a wide range of projects. The different funding modalities used by FONADIN include several financial alternatives such as guarantees, mezzanine loans and capital.
FONADIN's action plan for 2014 includes:

Supporting PPP project development
Exploring new alternatives to channel in a more efficient manner local institutional investors' resources (mainly pension funds) to infrastructure (project bonds, securitization, among others)
Strengthening project preparation and structuring in order to consolidate a pipeline of bankable projects for private sector investment, fostering solid evaluations and risk management techniques
Implementing a mechanism to prioritize infrastructure project development, in order to meet the infrastructure strategy outlined in the National Infrastructure Program 2014-2018

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What indicator(s) will be used to measure progress?	• Total investment (public and private) in infrastructure fostered by FONADIN. • Annual number of projects supported by FONADIN, including number of investment funds in which FONADIN participates.
Explanation of additionality (where relevant)	This policy action is not related to past commitments.

2. Employment

• The New policy action:	Unemployment Insurance
Implementation path and expected date of implementation	The policy is currently under discussion by Congress. If, as expected, it is approved this year, its implementation would be considered in the budget proposal for 2015.
What indicator(s) will be used to measure progress?	Once the reform is approved, its progress could be verified by the number of applicants that are granted unemployment insurance in a given year.
Explanation of additionality (where relevant)	This policy action is not related to past commitments.

3. Competition

• The New policy action:	Implementation of the Anti-trust Reform, including the recently approved secondary legislation.
Implementation path and expected date of implementation	COFECE will be in charge of implementing the measures through its everyday operation.
What indicator(s) will be used to measure progress?	Implementation could be tracked through the number of resolutions that COFECE emits in a year.
Explanation of additionality (where relevant)	Secondary legislation defines several important details that complement the constitutional reform and enable its implementation.

• The New policy action:	Implementation of the Telecom Reform, including the recently approved secondary legislation.
Implementation path and expected date of implementation	The Telecom Reform has already been approved by Congress and is in its early stages of implementation. The Telecom Regulator (IFETEL) is now in charge of its implementation.

What indicator(s) will be used to measure progress?	Progress on this front could be tracked by the penetration of telecom services among the population (i.e. broadband access, cellphone penetration) and by price indicators (i.e. dollars per MB of broadband speed).
Explanation of additionality (where relevant)	Secondary legislation defines several important details that complement the constitutional reform and enable its implementation.

4. Any other structural policy

The new policy action:	**1. Complete the secondary legislation of the Energy Reform**
Implementation path and expected date of implementation	The Energy Reform aims at increasing private investment across the whole sector. The new legal framework will allow for substantive risk sharing between the private and public sectors, which will allow Mexico to fully profit from its energy potential. The Constitutional reform was approved by Congress in December 2013, nevertheless it is fundamental to complete the secondary legislation of the Energy Reform to ensure its full implementation. With this Reform, the Mexican Government will be able to perform exploration and extraction activities of oil and other hydrocarbons through contracts with PEMEX and/or the private sector. Private investment in oil refining and processing will be allowed, as well as in oil transportation, storage and the distribution of natural gas, gasoline, diesel and other oil derivatives. In addition, the private sector will be able to participate in all the petrochemical chain and to perform activities of generation and commercialization of electricity. The reform creates a Sovereign Stabilization and Development Fund, which will receive and manage oil revenues in order to promote sound public finances in Mexico. Moreover, the Fund will channel resources for long-term savings, the universal pension system, science and technology, infrastructure for development, among others. These actions will clearly contribute to growth and employment. The Energy Reform's secondary legislation was presented to Congress on April 30, 2014. This legislation is expected to be approved in mid-August 2014.
What indicator(s) will be used to measure progress?	Total investment in energy sector as percentage of the GDP.
Explanation of additionally (where relevant)	Secondary legislation defines several important details that complement the constitutional reform and enable its implementation.