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cutting through complexity

Mexico

High Growth Markets country profile

Mexico is the world's twelfth most populous country, the eleventh biggest economy and the fifth largest emerging market, thanks to a young and growing middle-class. Following slower growth in 2013, the annual rate of increase in gross domestic product (GDP) is expected to average 3.7 percent between 2014 and 2018. Meanwhile, demographic trends and rising urbanization should support a rapidly growing consumer market in the medium term. Mexico's natural geographical advantages provide considerable scope for developing infrastructure links, and should help the country become a manufacturing hub for investors focused on North and Latin American markets.

Country overview

Geography and climate

- **Location:** part of North America; shares common boundaries with the southern US
- **Climate:** varies from tropical to desert
- **Regions:** one federal district and 31 states
- **Major cities:** Mexico City (19.3 million), Guadalajara (4.3 million), Monterrey (3.8 million), Puebla (2.3 million), Tijuana (1.6 million)
- **Tier two cities:** Chihuahua, Guadalajara, Juarez, Queretaro, Tijuana

Political system

- **Type of government:** federal republic
- **Capital:** Mexico City

Population, language and religion

- **Population:** 116.2 million
- **Urban population:** 78%
- **Demographics:** 0–14 years: 28.0%; 15–64 years: 65.1%; 65 years and over: 6.9%
- **Median annual household income:** 18,574 US dollars (US$)
- **Official language:** Spanish
- **Prominant religions:** Roman Catholic

Currency and central banking

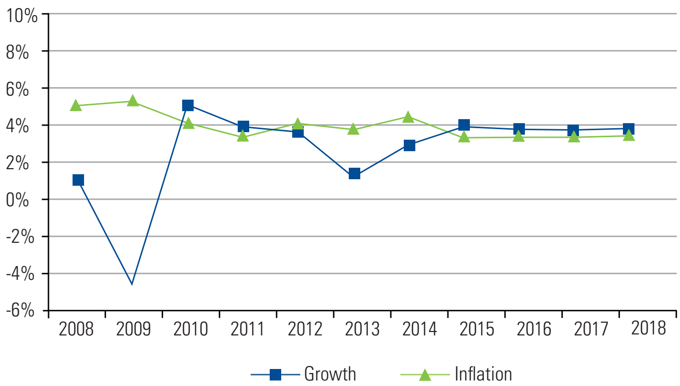
- **Local currency:** Mexican pesos (MXN)
- **Exchange rate:** 1MXN = US$0.0765 (1 April 2014)
- **Interest rate (average annual rate):** 3.5% (as of March 2014); 4.3% (2013); 4.8% (2012); 4.8% (2011); 4.9% (2010); 5.9% (2009)
- **Foreign exchange reserves:** US$167.1 billion
- **Total debt (2013):** external: US$354.9 billion; internal public debt: 37.7% of GDP (2013 estimate)

Business environment

Economic environment

- **GDP in 2013 was US$2.1 trillion and is expected to grow by 3.7 percent annually** from 2014–2018; with some upside risks linked to the short-term structural reforms that should improve competitiveness. The median household income is expected to increase to US$24,398 by 2017.
- **Foreign direct investment (FDI) (billions):** inbound: US$27.9 (2008); US$35.2 (2013); US$46.1 (2018–forecast); outbound: US$1.2 (2008); US$10.0 (2013); US$22.1 (2018 forecast)
- **Exports free on board (FOB) (billions):** US$371.4 (2012); US$380.9 (2013); US$565.1 (2018 forecast)
- **Imports FOB (billions):** US$371.2 (2012); US$381.6 (2013); US$572.6 (2018 forecast)
- **Sector breakdown:** service sector: 62%; industrial sector: 36%; agriculture sector: 4%
- **Trade balance (billions):** surplus of US$0.2 (2012); deficit of US$0.7 (2013); US$7.6 (2018 forecast)
- **Stock exchanges:** BMV (125), MexDer

GDP growth and inflation (average consumer price index (CPI))



Source: Economist Intelligence Unit, 2014

Investment climate

Key considerations

- **Fiscal and monetary policy:** Conservative fiscal and monetary policies underpin macroeconomic stability. However, a weak, non-oil fiscal revenue base, combined with shallow credit markets leave the authorities with few tools to boost demand. Pressure on the fiscal accounts has so far been neutralized by high international oil prices, but more comprehensive reforms are needed to reduce the dependency on oil revenue. The government will increase spending in 2014–2018, while fiscal reforms approved in 2013 should raise GDP by almost 3 percent by 2018. Despite occasional spikes, inflation is expected to remain below the 4 percent target ceiling set by the central bank – Banco de México. Monetary authorities will maintain a positive stance, prioritizing growth. Tax reforms will aim to reduce the burden of tax collection currently placed on large companies and allow for greater public spending on human capital.
- **Competition policy:** During 2014–2015, new regulations should tighten enforcement of competition policy, particularly in the telecommunications sector. Between 2016–2018, the government will attempt to reduce red tape and expand deregulation schemes for business.
- **FDI policy:** The opening-up of the telecommunications and energy sectors is likely to boost foreign direct investment, following fairly weak inflows in the years 2009–2012. In 2014–2015, the government is set to pursue an open policy towards FDI, modernizing the state oil firm, Petróleos Mexicanos, with better terms offered to public-private partnerships. Concession contracts are also expected in the energy sector. In the period 2016–2018, the automotive and aerospace industries should be bolstered by the creation of centers of design. To encourage geographical and sectorial FDI diversification, Mexico is developing stronger investment links with the European Union (EU), Asia and Latin America, and opening up its energy and telecommunications sectors.
- **Foreign trade and exchange controls:** Mexico boasts one of the world's largest networks of trade agreements, linking it with more than 40 countries across three continents. Despite these connections, exports to the US still accounted for 78 percent of total exports in 2012. The Trans-Pacific Partnership (a proposed trade agreement between Australia, Brunei, Chile, Canada, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the US and Vietnam) should bring greater diversity, although trade with the US will continue to dominate during 2014–2015. There is also likely to be further progress on a free trade agreement (FTA) with Brazil. Tariff and non-tariff barriers are expected to fall, although quotas persist for sensitive products. Between 2016 and 2018, a wide network of FTAs, along with greater investment by China should lead to more sustained export growth.
- **Financing policy:** In the period 2014–2015, banking reforms should improve access to financing for small and medium-sized enterprises. Between 2016–2018, the market for debt and equity issues is likely to grow faster, due to expansion of investment portfolios, as well as greater investment flexibility of private pension funds, following laws passed back in 2008. The development bank sector is also expected to expand.
- **Taxes**: A number of recent tax reforms have been designed to simplify the tax code, consolidate corporate taxes and eliminate the flat-rate business tax ('Impuesto Empresarial a Tasa Única'). Under the new tax code, Mexico retains a 30 percent corporate income tax rate, which is set to fall to 29 percent in 2014 and 28 percent in 2015. There is an additional corporate income tax of 10 percent on profits and dividends paid to Mexican individuals and foreign residents. Ten percent income tax is imposed on capital gains on the sale of shares for foreign residents – a group that was previously exempt. Expect the Mexican government to continue to attempt to bring more of the 'informal' economy into the tax base – a strategy that is essential to setting the public finances on a more sustainable path.

KPMG in Mexico

KPMG member firms are among the world's leading providers of Tax, Audit and Advisory services. In Mexico, KPMG has approximately 2,000 professionals and 16 offices.

KPMG in Mexico aims to respond to complex business challenges facing customers and to take a comprehensive approach that spans professional disciplines, industry sectors and national boundaries.

For more information, please visit the KPMG in Mexico website: kpmg.com/mx

Sources: Economic Intelligence Unit, 2014; Central Intelligence Agency, 2014; KPMG International research, 2014; Everest Group, 2014; Market Watch, 2014

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