2016

GROWTH STRATEGY

MEXICO

A. Economic Context and Objective

Economic Objective

The approval and implementation of a comprehensive structural reform package during the past three years strengthened Mexico's position to further promote strong and sustainable economic growth. Eleven structural reforms were designed, among several objectives, to boost productivity in key economic sectors, namely: Energy, Telecom, Financial, Fiscal, and others. Nonetheless, this template addresses only a subset of reforms, as key commitments, that was initiated in the relevant G20 period. Going forward, Mexico will proceed with the implementation of the full reform agenda.

Mexico's strong macroeconomic framework will contribute to mitigate any possible negative spillovers that could arise from the complex international environment. Increased financial volatility and emerging risks threaten the global economic recovery. Emerging Market Economies (EMEs), even those characterized by very strong fundamentals, have become more vulnerable to external shocks. Recently, downward risks have increased considerably, largely explained by the following factors, several of which can be mutually reinforcing –particularly in the way they affect EMEs: 1) the increased magnitude of external shocks and the amplification of their transmission channels onto EMEs, including Mexico; 2) further deceleration of world trade and overall global economic activity; 3) uncertainty around the monetary policy stance in advanced economies resulting in higher financial volatility; and 4) the emergence of potentially significant risks in the global economy, particularly, the rising specter of protectionism.

Against this background, Mexico maintains its commitment to: macroeconomic stability, while enhancing its resilience to external shocks; the steady and timely implementation of the structural reforms, including the ongoing fiscal consolidation trajectory; the continued anchoring of inflation expectations; the gradual rebuilding of reserve buffers; and a strong oversight of the domestic financial system.

Current and Future Growth Prospects

The information available for 2016 indicates continued economic growth in Mexico due, in part, to a strong domestic demand, particularly driven by consumption and investment. GDP in the first and second quarters of 2016 grew, year over year, at 2.5% and 1.5%, respectively. This growth took place under an adverse external environment as global growth expectations have been further revised downwards.

Despite the slack in global demand, domestic demand in Mexico continued to expand at a steady pace and is expected to keep supporting economic activity over the next quarters. Growth in domestic expenditure has been mainly driven by low inflation –that contributed to a recovery in the real wage bill–, the improvement in the labor market and the implementation of structural reforms; all of these factors are expected to prevail during the next quarters. As a result, domestic demand dynamism has managed to partially offset (and is estimated to keep doing so) the weakness in external demand, so that Mexico's economy is expected to continue growing.

In the medium term, the aforementioned reform agenda along with other structural changes currently underway will positively impact investment levels. Particularly, the enacted reform agenda is expected to better the investment climate through an enhanced regulation that provides new instruments and opportunities, in order to improve legal certainty for private investment in the energy, telecommunications and financial sectors. Structural reforms have begun to affect growth, mostly through their impact on investment and competition. Furthermore, the full impact of the reform agenda will most likely play out in the medium term through increases in productivity, deeper market competition, lower prices for consumers and the liberalization of strategic sectors.

Assessment of Obstacles and Challenges to Growth

Mexico's economic growth and macroeconomic stability faces a complex external environment: (i) a global economic slowdown; (ii) relatively low oil prices, in spite of their recent relative recovery; (iii) divergence in monetary policy stances in advanced economies, which could increase volatility in financial markets; in particular, US monetary policy normalization; and (iv) other recent international developments which could also increase downside risks to growth, such as a further deceleration in world trade.

Regarding domestic factors, a handful of elements restrained productivity growth in the past years, thereby limiting Mexico's growth potential. Low levels of competition were perceived in several strategic input markets, while informality is still pervasive in some sectors of the economy. Despite the observed recovery, more progress is required in order to boost private consumption, including through credit, which has gradually improved in recent years. These and other obstacles to growth are addressed by the reform agenda initiated in 2013 and by other recent economic policy measures. The Mexican authorities are working so as to promptly implement the structural changes embedded in the reforms, for their benefits to be tangible in the near term.

B. Macroeconomic Policy Actions to Support Growth

For 2016 and onwards, Mexico's economy and public finances will continue facing a complex and volatile external environment.

Macroeconomic Fundamentals and Risk Management Strategy.

Mexico is well-prepared to face a complex global environment thanks to its strong macroeconomic fundamentals, which, in addition to its risk management strategy, contributed to an orderly adjustment of its financial markets in periods of high volatility.

a) **The Flexible Exchange Rate Regime,** which serves as a buffer to attenuate the impact of adverse external shocks. In Mexico, the Foreign Exchange Commission (composed by the Ministry of Finance and the Central Bank) is responsible for conducting the foreign exchange policy. Various elements have strengthened the role of the exchange rate as a buffer against the referred shocks. First, in recent years there has been a reduction in the pass-through of exchange rate fluctuations to domestic prices. Second, there is a well-developed derivatives market in Mexico, which allows economic agents to hedge 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. In February 2016, the Foreign Exchange Commission moved from an auction-based to a discretionary intervention setting, triggered only under extraordinary circumstances to support orderly and liquid market conditions. The flexible exchange rate regime will continue to act as the key shock absorber during periods of global financial turmoil.

b) **An Autonomous Central Bank with a Credible Monetary Policy** and well-anchored inflation expectations. The Central Bank of Mexico's constitutional mandate is to pursue the stability of the purchasing power of the national currency. To meet this objective, Banco de México adopted an inflation-targeting scheme as a framework for the monetary policy conduct. Specifically and consistent with its mandate, the Central Bank has established as a permanent target an inflation rate of 3 percent (with a variability interval of plus/minus 1 percentage point) 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, thus reducing the level, volatility and persistence of inflation. Throughout 2015, inflation was temporarily reduced to a level below the permanent inflation target of 3 percent, but within the variability interval, and in 2016, it is expected remain close to its 3 percent target. The Central Bank is fully committed to adjusting the policy interest rate as necessary to keep inflation in line with the target in the medium term.

c) **A High Level of International Reserves** (177 billion dollars) and a Flexible Credit Line (FCL) with the IMF (around 88 billion dollars). The increase to the IMF FCL agreement, approved on May 27, 2016, will serve to enhance the protection of the economy and "give confidence that Mexico's economic policies will remain strong" amid a volatile and uncertain environment (IMF, Press Release No. 16/250, 2016). In this sense, the renewal of the FCL is a sign of confidence from the international community to Mexico's economy and an integral part of the strategy in the responsible management of macroeconomic policy.

d) **A Solid and Well-capitalized Banking Sector** in full compliance with Basel III requirements.

e) **The Oil Price Hedge** that insures federal government revenues against sudden drops in international oil prices.

f) **A Public Debt Policy that Diversifies Risks** and assures a trajectory to low and stable levels.

g) **A Timely and Responsible Fiscal Strategy**. The Federal Government has the strong commitment to preserve solid public finances. In this regard, a fiscal consolidation process was committed to in 2013, implemented in 2014 and 2015, in order to finally achieve a steady state in the fiscal balance in 2017, one year before the expected date. In 2015, all fiscal balance targets were met:

- Public Sector Borrowing Requirements (PSBR), the broadest measure of fiscal balance which considers the financing needs of the Federal Government and public sector entities, stood at 4.1% of GDP in 2015. The PSBR decreased by 0.5% of GDP with respect to the ones observed in 2014. It is estimated that in 2016 PSBR will be 3.0% of GDP, which means a reduction of 1.1 percentage points of GDP compared to the end 2015 and 0.5 points of GDP compared to 2016 Economic Program.

- Total public deficit amounted to 3.5% of GDP; excluding productive investment, the deficit was 1.0% of GDP, which fulfilled the goals approved by the Congress and the required budgetary goal in order to achieve a steady state in 2017. The government updated its primary balance estimate for 2016 to a deficit of 0.4% from a previous estimate of 0.6% of GDP. For next year, it is projected a primary surplus of at least 0.2% of GDP, the first surplus since 2008.

- Regarding Banco de México's operating surplus, in 2015, the President sent to Congress an amendment to the Federal Budget and Fiscal Responsibility Law (LFPRH), which established a specific purpose for Banco de México's operating surplus that ensures a responsible use of these resources. In this sense, the allocation of the operating surplus will be reflected in an improvement of the PSBR and the Historical

Balance of the Public Sector Borrowing Requirements. According to this Law, at least 70% of these resources should be used to amortize debt in advance or decrease debt issuance requirements during the fiscal year. The remainder should be used to support the financial position of the Federal Government (it reduces Public Sector Borrowing Requirements), namely through the Budget Stabilization Fund. This measure reinforces the Central Bank's autonomy, and avoids funding permanent spending with non-recurrent resources. The Central Bank sterilizes any monetary impact that may arise from this operation.

For 2017, the Federal Government is committed to the multiannual goal of fiscal consolidation. According to the General Economic Policy Preliminary Guidelines for 2016, the Government anticipated an adjustment of programmable expenditure of 0.9% of GDP, excluding high economic and social impact investment (in addition to the preemptive expenditure cuts of 0.7% and of 0.2%, announced in February and in June 2016, respectively). It is worth mentioning that current fiscal projections for 2016 and 2017 were made using very conservative assumptions for the oil price at 25 dollars per barrel in 2016 and 35 dollar per barrel in 2017.

It is important to consider that the General Economic Policy Preliminary Guidelines document is based on specific macroeconomic premises and foresees the accomplishment of the public finance objectives of the Economic Program for 2016 and 2017. These premises will be updated in a timely manner in order to integrate the Federal Budget proposal for 2017, to be submitted to the Congress in September.

In this way, the Federal Government will maintain the policy of no tax increases and will not resort to higher indebtedness, against the prospects of continued low oil revenues. Therefore, the Government will make the necessary fiscal adjustments to meet the goal of fiscal consolidation.

During 2016, Mexican authorities have made four relevant announcements to further strengthen public finances and to ensure macroeconomic stability.

Firstly, on February 17, the Ministry of Finance and Banco de México announced coordinated measures regarding monetary and fiscal policy in order to respond comprehensively to deteriorating conditions in the global environment. In this context, the Government acted responsibly in order to further strengthen its macroeconomic fundamentals, meeting the established goals of the fiscal balance and acting in coordination with Banco de México. These measures consisted of a preemptive fiscal adjustment of 132.3 billion pesos (0.7% of GDP), and a budgetary adjustment for Pemex of 100 billion pesos.

Secondly, in April 2016, Banco de México announced the delivery of 239 billion pesos to the Federal Government on account of their operating surplus, corresponding to the 2015 fiscal year. In accordance with the Federal Budget and Fiscal Responsibility Law, these resources are to be used to reduce debt and improve the financial position of the Federal Government. Of the total amount, 70% are to be used to repurchase Federal Government debt and to reduce the issuance of Federal Government debt during 2016. Of the remaining 30%, 70 billion pesos are to be transferred to the Budgetary Revenues Stabilization Fund (FEIP).

Thirdly, the Federal Government announced measures to strengthen the financial position of the public oil company (Pemex).

Finally, in light of the increased financial volatility caused by the vote in favor of the United Kingdom leaving the European Union, on June 24, 2016, a second preemptive adjustment was announced, exclusively within the Federal Government, by 31.7 billion pesos, of which 91.7% correspond to current expenditure, and which affected neither beneficiaries of social programs, nor the national security budget.

Other Measures

Gasoline price policy. The Excise Tax (IEPS) on gasoline was designed using a variable rate in the 1990's. This rate served as a mechanism to reduce the effects associated to the volatility of international benchmarks. It was calculated on a monthly basis as the difference between the price fixed by the Federal Government on gasoline and the international benchmarks. As a result of the observed spread, the IEPS for gasoline and diesel was negative from 2006 to 2013. For the last 10 years, this implicit subsidy has represented around 7% of GDP. In 2008, the subsidy reached its highest point (223.7 billion pesos), which amounted to 1.83% of GDP.

Afterwards, due to the drop in oil prices, the gasoline and diesel IEPS became again a positive tax at the end of 2014. In 2015, the gasoline and diesel excise tax collection amounted to 193,763.9 million pesos (1.07% of GDP).

The gasoline and diesel IEPS scheme was prone to misalignments that could generate a negative excise tax, and, therefore, an inefficient fossil fuel subsidy. Since January 2008, the government committed to eliminate it. In order to achieve this goal, on January 1, 2016 the Federal Government implemented a policy of sliding prices for gasoline and diesel, which will be allowed to float within a band, following a transition scheme towards full liberalization in 2018, thereby reducing the gap between domestic prices and international benchmarks.

Measures to promote savings, investment and formalization during 2016

a) **Measures to promote savings:** (1) substitution of the current fixed withholding rate for paid interest with a formula that is updated annually; (2) exclusion of contributions to long-term saving instruments from the personal deductions' total limit; and (3) a program for capital repatriation, which considers the payment of the regular income tax rate, but no waivers of Anti-Money Laundering (AML) regulations.

b) **Measures to promote investment:** (1) immediate deductibility of investment for 2016 and 2017 for Small and Medium-sized Enterprises (SMEs), in the transport infrastructure and in the energy sectors; and (2) stimulus to medium-term reinvested earnings for firms, through a lower dividend tax schedule.

c) **Measures to promote formalization:** (1) a fiscal lottery every four months for those who make purchases with electronic bank payments; (2) use of fiscal information for credit pre-qualification of SMEs; and (3) more flexible requirements for the Fiscal Incorporation Regime (broadening coverage, eliminating restrictions to family members, and updating the income tax rate).

d) **Other sector measures:** (1) stimulus for investment in renewable energy; (2) investment in electricity generation; (3) stimulus to diesel usage in all industrial sector activities; (4) speeding up the process of deconsolidation; (4) food tax (IEPS) reimbursement for exports.

New financial vehicles will be introduced to complement public investment and channel large-scale capital, with the best international standards in terms of corporate governance, transparency, and participation of national and foreign investment:

a) **FIBRA E** (similar to a Master Limited Partnership): it is a market financial instrument that allows to invest in mature projects of energy and infrastructure sectors. The instrument's main characteristics are the following: (1) it will release resources for investment in new projects, (2) it will be offered directly to the general public, and (3) it will maintain high standards in transparency for fiscal purposes. On October 21, 2015 the regulation that completed the legal framework for this instrument came into force.

b) **Investment Project Certificates:** it is a market financial instrument with corporate governance and similar design to Private Equity Funds worldwide. The instrument's main characteristics are: (1) it is designed for foreign and local institutional investors and, in this sense, individuals may enjoy the returns on private capital through AFOREs (pension funds) and (2) it gives operational flexibility to invest in a wide range of industries with different risk exposures (capital-debt, mature or development projects).

On January 4, 2016, the National Commission for the Pension System (CONSAR) modified the law so that pension funds could invest in the new financial vehicles. On April 25, 2016 CONSAR established the prudential guidelines that must be followed by pension funds to invest in the Investment Project Certificates (CERPI) and Fibra E.

c) **Educational Infrastructure Certificates:** these are trust certificates, funded by the Multiple Contribution Fund of Federal States (FAM). The FAM provides a stable flow of resources, making it easy to project. The portfolio of educational improvement projects has been defined at 50 billion pesos. It will benefit more than 5 million students and over 33 thousand schools. It is worth mentioning that it possesses high standards of transparency, which are required to participate in the Mexican Stock Exchange.

The program is already in operation, with a first placement by 8.6 billion pesos (December 3, 2015) and currently attending 1,118 schools (as of February 29). On February 23, the government presented a website where the progress on schools under the program can be monitored: (www.inifed.gob.mx/escuelasalcien). A second roadshow took place to issue an additional 5 billion pesos.

Reforms on Corruption and Rule of Law

a) **Transparency.** On July 18, 2016 the President enacted the National Anticorruption System legal framework, the goal of which is to create strong and autonomous institutions to prevent and sanction corruption, as well as to cut red tape and to promote transparency of public works and services. The Transparency Reform entails the creation of a National Anticorruption System that will function as a coordination instance between authorities at all government levels in charge of the prevention, detection and sanction against corruption, as well as the control and audit of public resources.

The reform also envisages an Anticorruption Prosecution Office and specialized court rooms at the Federal Court of Administrative Justice, as well as the expansion of powers of two agencies, the Federal Government Audit Authority (which audits the use of public funds) and the Ministry of Public Administration (the Minister of which will now be ratified by the Senate). Under the new law, the two institutions will now have greater auditing powers and the faculty to investigate and act upon citizens' complaints and to take their findings directly to an administrative court. Also, criminal sanctions for acts of corruption are increased and termination of ownership of illegally obtained assets from corrupt public officials is contemplated.

In terms of Transparency, the Reform enclosed the approval of seven main laws: the General Law on the National Anticorruption System; the Law on Administrative Responsibilities; the Organic Law of Federal Court of Administrative Justice; Federal Penal Code; Organic Law of the Attorney General's Office; the Law of Oversight and

Accountability and the Organic Law of the Federal Public Administration. Legislators discussed and approved the laws mentioned above during an extraordinary session in Congress that took place in the period of June 13-17, 2016.

The OECD has welcomed Mexico's National Anticorruption System, assuring that the promulgation of these laws substantially transforms the anti-corruption legal framework. According to the OECD, "[…] perhaps the most important game changer of the reforms is that they reach beyond the Federal level and include all levels of government. Indeed, the new legislation requires the Mexican States to follow suit with their own local anti-corruption systems, thereby tackling some of the strongest footholds of corruption in Mexico." (statement from the OECD made on August 1, 2016)

b) **National Criminal Procedure Code** reform unifies the criminal justice model which allows our system of justice to transition towards a model shared by the Federation and the states, in order to (1) facilitate coordination among authorities; (2) increase investigation effectiveness at the federal and local levels; (3) provide greater legal certainty regarding the decisions of judges and courts; and (4) prevent the diversity of rules from creating scope for impunity. This code includes a new system of oral adversarial criminal justice.

   The new Justice System enacted in the reform has already been implemented at a federal level in all of the 32 states. The seventh and the last stage of nationwide implementation began on June 14, 2016, with the last 4 states to achieve a full operation status.

c) **The Political-Electoral Reform** changes the relationship among the branches of the government, and between the government and citizens in two main ways: (1) it modernizes institutions belonging to the political system to promote a better balance among the branches of government, facilitate dialogue and enhance agreements, and (2) it transforms institutions and electoral competition rules to strengthen citizen participation and to provide greater certainty regarding polls, both nationally and locally. The Political-Electoral Reform modernizes rules and electoral institutions to standardize the quality of democracy throughout the country. It also boosts the state capacity to reach agreements on the most important decisions, consolidating a results-based democracy for Mexicans.

d) **The New Appeal Law.** The Reform will expand the protection provided to citizens' rights, in order to make the administration of justice more expeditious and effective; to simplify and to modernize the legal process, and to strengthen the Judicial Branch of the Federation. The Injunction Law Reform has three main axes: (1) it expands the sphere of the protection of rights (i.e. human rights granted in international treaties will receive direct protection); (2) the effectiveness of Mexican justice increases (i.e. filing for an injunction can now be done online using the Electronic Signature); and (3) it strengthens the Judicial Power of the Federation, particularly the Supreme Court of

Justice (i.e. the Court is empowered to remove from office and to report to the District Judge both the authority responsible and their immediate superior if they fail to comply with an injunction sentence).

Measures to foster balanced and inclusive economic growth

Special Program to Democratize Productivity. In 2013, the Federal Government announced a special program to optimize factors involved in goods' production and services provision with the help of an advisory body, the National Productivity Committee.

The Committee has the following powers: (1) undertake a national diagnosis of the requirements for raising productivity and competitiveness in every sector and branch of production; (2) suggest alternative technologies and forms of work organization; (3) make recommendations for training plans and programs; (4) study mechanisms and new forms of remuneration to link workers' income to productivity; and (5) issue opinions on the destination and implementation of budgetary resources aimed at increasing productivity.

The Special Program to Democratize Productivity is based on four areas: (1) encourage the efficient use of production factors, through actions to encourage formal employment, expand credit and make more efficient use of the national territory; (2) promote the country's business environment through increased economic competiveness, legal certainty and investments in strategic sectors as well as a simpler, more straightforward tax system; (3) raise productivity within companies, through investments in human capital, as well as innovation and technological development processes; and (4) boost productivity in every region and sector of the country through programs and infrastructure projects that meet their specific needs. Raising and democratizing productivity is the best way to grow the economy and, more importantly, to increase family incomes.

Special Economic Zones Act. In September 2015, the President sent to Congress an Initiative for the creation of Special Economic Zones (SEZ) that (1) aims to increase productivity, (2) boosts employment and (3) creates wealth in regions with less economic development. The Initiative includes: (1) provision of fiscal, commercial and financial benefits, jointly with specific regulation and the development of economic infrastructure; (2) the government will provide certain flexibility in each zone to establish specific incentives and customs regime, tariff policy and merchandise control, depending on the initial condition and productive orientation of the region; (3) to ensure procedure efficiency and cut red tape, there will be coordination and cooperation among the three levels of government to facilitate the establishment and operation of new enterprises and (4) the Special Economic Zone will have provisions that will guarantee high standards in transparency and accountability. The goal is to develop regional value chains, expand local public services and provide benefits for both SEZ populations and neighboring communities. The medium- and long-term goal is to trigger productivity of the southern region and to establish the structural conditions that will generate more wealth and opportunities for integral development.

The Special Economic Zones initiative is already being implemented. In May 2016, the President decreed the creation of the first Special Economic Zone, and enacted the Federal Law on Special Economic Zones, which concluded the legislative stage and marked the start of the implementation phase. Also, the regulation was published in June, so that Special Economic Zones will be in place by the end of the year. The Law included the creation of the Federal Administration for the Development of Special Economic Zones, a decentralized agency of the Ministry of Finance, in charge of the implementation phase of the SEZ. This body now has regulation, planning and promotion functions of the SEZ in accordance with the best international practices. The head of this agency was also named in June.

The first three SEZ are Lázaro Cárdenas, Puerto Chiapas in Mexico's southernmost state of Chiapas, and the Isthmus of Tehuantepec. In addition, a zone in the "Oil-belt states" of Tabasco and Campeche is planned for 2017. Each zone will have a Master Plan, with elements and general characteristics of infrastructure and services associated with the area, which will be reviewed and adjusted every 5 years.

The deadlines for the implementation stage of these projects are as follows:

- By January 2017, the design and approval of the institutional legal framework is to be completed.
- By March, the approval of development programs by the Interministerial Commission and the signing of coordination agreements with states and municipalities will take place.
- By June, the opinion, declaratory, licensing and assignments should be in place.
- In October, the construction and operation of the Zones will begin; and
  By September 2018, an anchor tenant, such as an industrial company that can attract suppliers and others, should be in place for each zone.

C. Structural Reform Priorities

Currently, a major challenge is to ensure full and effective implementation of the approved structural reform agenda. Nonetheless, this is a process that will take several years. It is important to note that productivity has been the axis of the agenda. In this context, the current Administration has prioritized the expansion of high productivity sectors, and also the integration of less productive ones to high-value chains to further boost Mexico's productivity. The role of the structural reforms is to support the links between a more efficient resource allocation, better-integrated global value chains, and productivity growth. Against this background, the structural reforms also aim to increase the quality of education through the Education Reform; which has a long-run impact on productivity while being key to promote inclusive growth.

C1. Implementation of Past Growth Strategy Commitments

Despite a complex and adverse external environment, Mexico's economic growth has been steady between 2-3 % from 2014 to 2015, especially when compared to other economies in Latin America.

As mentioned above, the Mexican authorities have been pursuing an increase in productivity, through the implementation of the structural reform agenda, while maintaining strong macroeconomic fundamentals and sound public finances. Since 2015 and even more through 2016, the effects of the structural reforms have been observed. There are four main structural reforms:

The Energy Reform. This reform, on the one hand, has substantial implications for the government and public finances. In addition, it has changed the landscape in oil activities such as exploration and production, but also in power generation. The national oil company, Pemex, needed to make that adjustment to better face volatile oil prices. The energy reform is an opportunity to change and improve in many areas. The company will have at its disposal the economic, legal and financial instruments that other integrated oil companies have, with the possibility of associating with and bringing in private capital as well as sharing risk more efficiently. Pemex has the opportunity to bring in national and internationally qualified partners and take advantage of different technologies, and innovate in risk management strategies. Going forward, this will be a game changer for a more efficient energy sector.

In sum, there are new legal and financial instruments, to a sector that has opened up to private investment and the government has put in place other policies and measures to interact with and complement the energy reform. Regarding the gasoline and diesel import policy, it is worth mentioning that since April 1, 2016, Mexico has opened up to freely import gasoline and diesel, thus getting ahead to the original opening scheduled in 2017, which is a major change in the energy reform schedule, reflected in Annex 2.

Financial Services and Financial Sector Reform. Mexico's economic strength reflects a degree of diversification and improved growth prospects associated with structural reforms in key sectors, including in the financial sector. While economic growth remains subdued presently in line with current external headwinds, Mexico's stable long-term economic outlook will continue to contribute to a supportive operating and business-conducive environment for banks.

The financial sector remains sound, underpinned by a strong regulatory framework. Banks are profitable, well-capitalized, liquid and resilient to credit and market risks. The banking sector's loan portfolio is well-diversified by industry and loan type. One central challenge for the sector is the low-banking penetration. In this regard, banks and other financial institutions have new instruments and a legal framework to take advantage of the additional space for financial intermediation, which would also lead to a more inclusive financial system. In addition, one important effect of the reform is that it has already favored more competition in the sector, leading to better financing conditions and terms for financial services' users. Several interest rates, including for households and corporate loans, have been decreasing in the past years.

Among the main outcomes of this reform is higher domestic financing to the private sector, which increased from 25.7% in 2012 to 32.4% in the first quarter of 2016. In addition, domestic financial savings grew from 55.8% to 66.9% over the same period. The current loan portfolio to the private sector went up 12.7% in real annual terms in June 2016.

These accomplishments and the regulatory improvements were acknowledged by the World Bank's publication *Doing Business*, in which Mexico moved up from the 42nd to the 38th place. Within, in the Ease of Getting Credit category, Mexico went from the 12th to the 5th position. Going forward, this reform should weigh significantly on growth.

Telecommunications. The process to implement the telecommunications reform has been successful, in the sense that it has made the market credibly contestable and with a robust legal framework, so that it has brought in important outside players. The reform increased competition, which is already reflected in a drop in telecomm prices. In December 2014, long-distance and cell phone rates declined almost 50%, and competition has consistently continued throughout 2015 and 2016. Mexico is now not very different from most advanced economic markets in terms of having about three main market players. The level of competition seems to be in equilibrium in these markets and Mexico is now part of the big trend for the telecomm market competition.

Since the reform came into place, there are visible results such as lower telephone rates, the entry of new market competitors and higher penetration nation-wide of telecomm services. First, in the period of June 2013 to April 2016, long-distance rates decreased by 40.3%, cell phone rates fell 35.2% and fixed rates declined by 4.4%. Second, since 2015, there have been new players in the telecomm market, namely: AT&T (investment size: USD 7.4 billion), Eutelsat (USD 831 million) and Virgin Mobile (USD 45 million). Finally, there is higher market penetration of services, for instance, mobile broadband penetration has raised 57.5 million users, which represents a 409% increase and 54 million internet users, which amounts to an increase of 20% during the aforementioned period.

Fiscal Reform. Regarding our fiscal stance, the fiscal reform enacted in 2013 has been fundamental. Public finances have recently suffered a negative shock, which has been partially offset by the positive impact of the reform. On the one hand, Mexico's public finances were buffeted by the fall in oil revenues, as prices fell 70% and oil production continued declining for the past three years, particularly last year. On the other hand, the tax reform has helped Mexico reduce a 30 year-dependence on oil. In fiscal terms, only four years ago, Mexico still had 39% of revenues coming from oil, and now it is only about 19%. The fall in oil prices has been partially offset by a very important increase in tax revenues from about 8.4% in 2012 to 13% of GDP by the end of 2015. The levels and the robustness of our fiscal stance show that the economy is now significantly less dependent on oil prices, which reduces the exposure and risks in the medium term. Overall, the fiscal reform proved to be a timely policy as it helped to mitigate the effect of declining oil prices.

C2. New Structural Reform Measure

Responsible public finances to strengthen macroeconomic stability. In the current adverse environment, the objective is to preserve macroeconomic stability by acting responsibly and securing fiscal sustainability in the long term. As a result, the Federal Government is currently implementing a multi-year public spending adjustment plan. This adjustment aims to preserve the path of public finances through a fiscal consolidation, in a context of increased volatility in global financial markets and lower oil prices. With this strategy, we are establishing conditions for a timely reduction in public spending to ensure an orderly decline in financing requirements for upcoming years, while assuring the sustainability of public debt.

Despite the adverse global environment, the Mexican economy continued to perform favorably. The weakening of global growth prospects, an additional decline in the price of commodities (particularly oil), the divergent monetary policy in advanced economies and geopolitical tensions pushed up volatility in global financial markets at the beginning of the year, although it decreased by the end of the quarter. Despite this volatility, a favorable economic growth rate was observed. In this context, both the Federal Government and the Central Bank have reinforced their commitments to sound public finances, strong macroeconomic fundamentals and well-anchored inflation expectations for the economy. In 2016, they have announced coordinated measures regarding the monetary and fiscal policy in order to respond comprehensively to, among other things, external shocks and their effect on public finances and on the current account.

D. Investment

Mexico's investment strategy includes concrete policies and commitments to improve the investment ecosystem, foster investment in infrastructure, and support SME financing. The implementation of these commitments is underway and will take place during 2016-2018, with positive effects beyond this date.

The Federal Government is working on the implementation of the Investment Strategy by promoting the following measures:

1. Strong commitment to fiscal discipline and macroeconomic stability, which is necessary for long-term investment projects.
2. A structural reform agenda that fosters private investment in key sectors of the economy, such as energy and telecommunications, including a financial reform that promotes competition and access to better and more competitive financing conditions.
3. Consolidation of a pipeline of projects. In particular, the National Infrastructure Program 2014-2018 includes a comprehensive infrastructure development strategy that aims to increase the country’s economic growth and productivity. This program considers more than 700 infrastructure projects to be developed over the next years, accounting for more than USD 550 billion of public and private investment.
4. A solid institutional and legal framework, including a Public Private Partnership Act that provides certainty to the public and private sectors on infrastructure projects.
5. An efficient set of new investment vehicles that can contribute to funding the projects of the National Infrastructure Program and develop an asset class for infrastructure.
   - FIBRA E, which is an instrument for cashing out mature infrastructure projects, including energy projects. This vehicle shares many characteristics with the Master Limited Partnerships (MLPs). This instrument facilitates investment in infrastructure and energy sectors.
   - Investment Projects Certificates (CerPIs), which emulates a typical private equity structure, allowing the participation of top global asset managers and local and international institutional investors.
   - Educational Infrastructure Certificates, which will be traded in the Mexican Stock Exchange.

6. The Federal Government is working, through the National Development Banks, on the implementation of different programs to facilitate credit access to SMEs.

Please refer to Annex 1 for the status of implementation of key commitments.

	Facilitators	Safeguards
Investment Ecosystem	**1 Supporting Improvements in Investment Climate** Macroeconomic stability Competition strategy and regulatory reforms Removing restrictions on FDI Strengthening public investment efficiency Promoting R&D and business startup **2 Facilitating Financial Intermediation** Promoting domestic financial savings Private sector financing tools (local debt market and capital market) Respective role of different actors (banks, inst. investors, corporate finance)	**3 Enabling Appropriate Legal and Institutional Settings** Rule of Law and public governance Preconditions for long-term investment Governance and incentives of financial intermediaries Adequate regulatory framework Openness and information sharing Responsible business conduct
Infrastructure	**4 Supporting Improvements in Investment Climate** Regulatory framework for infrastructure Strengthening Public Investment Inflation and foreign exchange risk management alternatives **5 Facilitating Financial Intermediation** Promoting long-term financing environment Developing financing vehicles Private equity/ project bonds Developing secondary markets Tax incentives **6 Mobilizing MDB Resources and Role of NDBs** Country led MDB programs Technical assistance and experience sharing Role of National Development Banks	**7 Enabling Appropriate Legal and Institutional Settings** Developing an adequate PPP framework Stable and consistent regulation Sustainable and clean energy **8 Project Spectrum: Project Planning, Prioritization and Process Development** Project identification and prioritization Project preparation / execution Procurement and contract management Ensuring quality of infrastructure **9 Addressing Data Gaps** Project availability Sharing project information

SMEs	**10 Facilitating Financial Intermediation** Movable collateral laws and registries Insolvency regimes Asset based instruments Securitization Banking sector competition Tax incentives **11 Mobilizing MDB Resources and Role of NDBs** Role of National Development Banks Technical assistance and experience sharing	**12 Enabling Appropriate Legal and Institutional Settings** Product development Non-bank SME financing settings Availability of early stage capital (seed, angel, etc.) Incentives to formality **13 Addressing Data Gaps** Information sharing (standardized data set) Payment system information SME data gap dissemination

Annex 1. Past Commitment – Brisbane and Antalya Commitments

Brisbane and Antalya Key Commitments for Monitoring Purposes

<table>
<tr><th>• The policy action:</th><th colspan="2">Energy Reform</th></tr>
<tr><td>Inclusion of the commitment in growth strategies</td><td colspan="2">This measure was included in the Brisbane/Antalya growth strategies.</td></tr>
<tr><td>Detailed implementation path and status</td><td>Interim steps for implementation</td><td>

In December 2013, the Mexican Government approved an Energy Reform that 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. Additionally, the electricity sector has been liberalized by ending the monopoly of CFE and by promoting competition from new entrants.
In August 2014, the secondary legislation of the Energy Reform was approved, including the following main themes:

i. Exploration and Extraction Contracts
a. The auction process for exploration and extraction contracts will be managed by the National Hydrocarbons Commission, and any firm can participate. However, the Ministry of Energy (SENER) determined 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) determined the economic terms of the contract.
ii. Energy Policy and Regulatory Bodies
a. The National Gas Pipeline Center (CENAGAS) is 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) is in charge of managing the National Electric System and operating the electric wholesale market.
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</table>

		iii. Regulation for Production Companies a. The figure of State Productive Companies (SPCs) is created with technical, management and budgetary autonomy as well as regulated independent bodies. This way, the main goal of SPCs will be to maximize economic rent for the state, with a more similar structure to a private company. b. As an anticorruption measure, SPCs must have complete information systems about their suppliers and contractors, which must be updated regularly. c. Pemex and CFE, as SPCs, will be subject to an annual evaluation, which will be made by a commissioner who has to be an independent expert. **iv. Opening of the Domestic Electricity Market** a. CFE will remain as an electric service provider for residential consumers and for small and medium commercial and industrial clients. These users will not see changes in the current way they pay or consume electricity. b. Electric plants, except those intended for self-supply or smaller than 0.5 Mw capacities, will require permission from the Energy Regulatory Commission (CRE) to generate electricity. • **Implementation of Secondary Legislation:** **1. Upstream** 1.1 “Round Zero” was completed. In this bidding process, Pemex put forward its request for the exploration areas and production fields. It established which oil fields are available for subsequent rounds of bidding. 1.2 An independent board for CFE and Pemex was selected and ratified by Congress. 1.3 The public invitation to bid (“Round 1.1”) for Exploration and Production (E&P) contracts was issued. 1.4 The public invitation to bid (“Round 1.2”) for Extraction in shallow waters was issued. 1.5 The public invitation to bid (“Round 1.3”) for Extraction in terrestrial fields was issued. 1.6 The first E&P contracts in shallow waters were awarded (“Round 1.1”). • Competitive terms for participants and transparency standards were unprecedented, which was acknowledged internationally.

		• Bidding: a winner was declared in 2 of the 14 tendered areas (11 offers were received for 6 areas). • The total income for the state per contract is estimated between 74%-86% in Block 2 and 83% -88% in Block 7. • Expected investment: minimum 150 million dollars and potential 2.7 billion USD (if exploration proves successful). 1.7 The contracts for the E&P shallow waters contracts were officially signed. 1.8 "Round 1.2": Shallow waters. Bidding: a winner was declared in 3 of the 5 fields tendered (fields 1, 2 and 4). • The total income for the state per contract is estimated at between 90%-92% in Block 1, and 82% -88% in block 2, and 85%-88% in Block 4. • Expected investment: 3.1 billion USD. 1.9 "Round 1.3": Terrestrial fields. • Bidding: a winner is declared in 25 of the 25 auctioned fields located in Chiapas, Nuevo Leon, Tabasco, Tamaulipas and Veracruz. • The average of the total income for the state per contract is estimated at 63% of gross income. • Expected investment: 1.1 billion USD. 2. **Electricity** 2.1 Independent system operator (CENACE) was created, removed from CFE and transformed into a public entity in charge of the national electricity system operation. 2.2 Legal framework for electricity generation competition was issued. 2.3 Guidelines and regulation issued for interconnection (CFE is allowed to engage in contracts with private parties for the operation of the distribution and transmission network). 2.4 Electricity market rules and clean energy certificates regulation were issued. 2.5 Regulatory basis for the functioning and operation of the electric market was issued.

		2.6 Electricity market will be in operation and functional separation of CFE in transmission, distribution and retailing. 2.7 First long-term electricity tender ▪ 11 winners and 18 selected proposals. ▪ Solar energy was the unquestionable winner of the tender, as 12 out of the 18 winning proposals are based on this technology, amounting to 1,771MW of the assigned energy with an average price of US$45.15 per megawatt-hour. ▪ The results obtained by solar energy in this first electricity tender enhance Mexico's position as one of the world's most attractive solar markets. Together, the 18 proposals represent 84% of the total energy originally requested by CFE, and 94.6% of the MX$5,380,911 worth of CELs offered in the tender. ▪ It managed to allocate most of the energy required by CFE at a lower price than expected. 2.8 The public invitation to bid for the second long-term electricity tender was issued. 2.9 Second long-term electricity tender. 3. **Downstream.** The creation of an independent operator for the gas pipeline system (CENAGAS). 3.2 Legal framework that allows competition in the following activities: transport, distribution and storage of refined and processed products, refining and production of petrochemical. 3.3 Retail sale of gasoline and diesel open to competition. 3.4 The excise tax on gasoline will be fixed and the price will be allowed to float within a band as a transition scheme towards liberalization in 2018. 3.5 Gasoline and diesel imports open to third parties.
	Deadline	The deadline for the implementation of the steps mentioned above: **1. Upstream** 1.1 August 2014. 1.2 September 2014. 1.3 December 2014. 1.4 February 2015. 1.5 May 2015. 1.6 July 2015.

		1.7 September 2015. 1.8 September 2015. 1.9 December 2015. 2.1 August 2014. 2.2 October 2014. 2.3 January 2015. 2.4 July 2015. 2.5 September 2015. 2.6 December 2015. 2.7 March 2016. 2.8 May 2016. 2.9 September 2016 3.1 August 2014. 3.2 October 2014. 3.3 January 2016. 3.4 January 2016. 3.5 April 2016, previously scheduled for January 2017.
	Status	• The Energy Reform is being implemented in a timely manner, it is in an advanced stage and all deadlines have been met.
Impact of measure	• This reform will have a sizeable positive impact on economic growth, investment and competition. • The cost of energy has started to gradually decrease as a result of the opening of the market for electricity generation, transport, distribution and storage of processed and refined products, as well as petrochemical activities. This will be reflected in a more productive economy. • The prices of gasoline as of January 2016 with respect to 2015 have decreased 3% for the first time in recent history. • Regarding electricity rates, since the reform came into force, rates have reduced as follows: -23.2% high voltage. -15.7% medium voltage. -2.1% Commercial and High Use Domestic Rate (DAC). -4.0% domestic rates at all levels. • The Energy Regulatory Commission (CRE) has granted 237 permits for electricity generation, within the new framework of the energy reform, which implies an average monthly increase of 2% in granting of such permits.	

<table>
<tr><th>• The policy action:</th><th colspan="2">Competition (Anti-trust) Reform</th></tr>
<tr><td rowspan="3">Detailed implementation path and status</td><td>Interim steps for implementation</td><td>• In July 2014, the new Economic Competition Law became official and aims to address the lack of competition in strategic markets. The main elements of the approved law are:
– New faculties of the Federal Antitrust Commission (COFECE), such as declaring and regulating essential inputs, determining and establishing measures to remove barriers to entry.
– New categories of absolute monopolistic practices and new regulatory measures to prevent and investigate market concentration.
– New special procedures and a modification of the Federal Criminal Code to include penalties for monopolistic practices.</td></tr>
<tr><td>Deadline</td><td>• The Federal Antitrust Commission (COFECE) has been in operation for three years now since 2013 and the new regulatory framework was established in 2014. Since then, the Commission has already made progress in investigating and sanctioning competition issues in various sectors, such as the financial, the aviation and poultry sector.
• All deadlines have been met.</td></tr>
<tr><td>Status</td><td>• The Federal Antitrust Commission was released in 2015, with its Strategic Plan for 2014-2017, which can be consulted through the following link:
http://www.cofece.mx/attachments/article/37/PE_2014-2017_act_2015.pdf
• Mexico recorded an increase of 10 places in the indicator that assesses the effectiveness of antitrust policies, known as the Global Competitiveness Index 2014-2015, compared to the year before, compiled by the World Economic Forum, rising from 114th to 104th place. In addition, the specialized magazine Global Competition Review, increased the performance rating of the Federal Antitrust Commission in 2015, from two and a half stars (acceptable performance) to three stars (good performance). It is the first time that the competition authority in Mexico gets this rating, which is shared with other jurisdictions such as Austria, Canada, Sweden and Switzerland.</td></tr>
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Impact of measure	• The Competition Reform, along with other approved reforms, will increase competiveness in markets characterized by a high degree of concentration. Also, it will reduce monopolistic practices.

• **The policy action:**	**Execute the National Infrastructure Program (NIP) 2014-2018**	
Detailed implementation path and status	Interim steps for implementation	1. Timely execution of the NIP during the present Federal Administration. 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 program includes 743 infrastructure projects to be developed between 2014 and 2018, which account for more than 550 billion dollars. 2. The construction of the New Airport of Mexico City (NAICM).
	Deadline	1. The NIP will be implemented during 2014-2018. 2. The NAICM is expected to become operational by 2020.
	Status	• The Federal Government is taking the necessary actions to continue with the timely implementation of the National Infrastructure Program. The 2016 Federal Budget was prepared using a zero-based budget approach, in order to give priority to investment projects. In addition, the Federal Government is currently analyzing ways to leverage private investment in infrastructure. • The construction of the NAICM started in 2015.
Impact of measure	• The execution of the NIP will improve economic activity and generate employment to support infrastructure development and productivity growth. • This program, together with the structural reform agenda will lead to an increase in the economic growth.	

• The policy action:	Strengthen the role of National Development Banks (NDBs) in Infrastructure and SME financing.	
Detailed implementation path and status	Interim steps for implementation	1. NDBs 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. Major NDBs (BANOBRAS, NAFIN and BANCOMEXT) will expand and induce credit for almost 45 billion USD through their mid-term plans, that include: - Fostering the participation of commercial banks in infrastructure financing. - 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. 2. A set of measures to support SMEs are being implemented, which include: i. The implementation of the Youth Credit Program. This program provides credit to entrepreneurs between 18 and 30 years old who want to start or expand a business. The program considers 4 financial products (more information is available at http://tuprimercredito.inadem.gob.mx): - Bank loan to start a business, from 3,300 to 10,000 USD. - Bank loan to start a business, from 10,000 to 33,000 USD. - Bank loan to expand existing businesses, up to 20,000 USD. - Bank loan of up to 166,000 USD to expand businesses with at least one year of operation. ii. The implementation of the National Entrepreneur Fund, to foster productivity and innovation in micro, small and medium enterprises. - The fund provides grants to financing micro, small and medium enterprises, including training programs, consulting services, quality certifications, product design, technology transfer, equipment acquisition, among others. - The amount of the grant could range from 10% to 100% of the total cost of the project.

		iii. The implementation of the “Crezcamos Juntos” program aims to incentivize SME’s to join formality by increasing its benefits: - To be registered in the program, enterprises must fulfil their tax-related obligations. - Different tax exceptions for the first ten years. - A 50% discount in health and social security fees. - Housing loans and consumer credits for employees. - Access to bank financing in order to increase the productive capacity of SMEs.
	Deadline	1. It is expected that major NDB’s will expand and induce credit for almost 45 billion USD by 2018. 2. Regarding measures to support SMEs: i. The Youth Credit Program is available since February 2015. ii. The National Entrepreneur Fund operates since 2014. iii. The “Crezcamos Juntos” Program started in September 2014.
	Status	• All measures are currently being implemented.
Impact of measure	• This commitment provides 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. • The measures to support SMEs will expand bank lending at better terms and conditions, strengthen their productive and technological capabilities, decrease informality and contribute to generate credit information.	

• The policy action:	Fostering Investment in Infrastructure through the implementation of the Financial Reform and the National Infrastructure Fund.	
Inclusion of the commitment in growth strategies	This measure was included in the Brisbane/Antalya growth strategies.	
Detailed implementation path and status	Interim steps for implementation	1. Implementation of the Financial Reform: i. Maintain a solid financial system: – New liquidity rules for banks and stress tests for banks and brokerage houses. – The Financial System Stability Council was created to coordinate and reinforce the soundness of the financial system. – The Bank for International Settlements (BIS) assessed the Basel III implementation commitments in Mexico and recognized that Mexico is one of the leading countries in their implementation. – The National Financial Inclusion Council was established to formulate, implement and monitor the national policy of financial inclusion. ii. Increase competition in the financial sector and improve the quality of financial services through regulations to inhibit anticompetitive practices and stronger attributions to the Federal Commission for Protection and Defense of Financial Services Users (CONDUSEF): – Elimination of abusive clauses in contracts from financial institutions such as tied sales. – The Bureau of Financial Entities was consolidated with information of entities and user claims. – The Registry of Debt Collection and Debt Recovering Offices (REDECO) was created. iii. Establish conditions to encourage private banks to extend credit, through: - Easing of the corporate regime of investment funds. - Modernization of the stock exchange market. - Establishment of a mechanism to evaluate banking institutions. - Improvement of regulations for commercial bankruptcy.

		- Establishment of a system of correspondents for the popular savings institutions in order to increase financial inclusion, even in places without banks. iv. Promotion credit through Development Banks, mainly by stronger corporative government, mandates and organizational structures for these NDBs. 2. The Mexican Federal Government is encouraging a reform of capital market regulation, regarding the participation of institutional investors such as pension funds and insurance companies in infrastructure, in order to: i. Improve incentives for investment portfolio management, leading to better investments and more efficient asset managers. ii. Simplify the regulatory framework for infrastructure products, making Development Capital Certificates (CKDs) a more flexible instrument. iii. Extend the range of institutional investors that can invest in CKDs, including insurance companies. iv. In September 2015, three new instruments were launched in order to foster institutional investors' participation in infrastructure financing: i) FIBRA E, which is a new asset class designed to monetize cash flows from stabilized energy and infrastructure project; ii) Investment Projects Certificates (CERPIs), that allow domestic and foreign institutional investors, including pension funds and insurance companies, to allocate resources in a wide range of industries with different risk exposures (capital, debt, mature or development projects); and iii) Educational Infrastructure Certificates, which will be traded through the Mexican Stock Exchange. The National Banking and Securities Commission and the National Commission for the Pension System circulated, for public consulting, the legal framework for FIBRA E and CERPIs. 3. Strengthening the National Infrastructure Fund (FONADIN), which is the main vehicle of the Federal Government to foster private participation in infrastructure. FONADIN's action plan aims to: i. Support PPP project development. ii. Implement a mechanism to prioritize infrastructure project development. iii. Strengthen project preparation and structuring in order to consolidate a credible pipeline of bankable projects for

		private sector investment, fostering solid evaluations and risk management techniques. iv. Strengthen its financial capacity.
	Deadline	1. Different involved agencies, including NDBs, the National Banking and Securities Commission (CNBV), the Federal Commission for Protection and Defense of Financial Services Users (CONDUSEF), among other federal agencies, will continue working in the implementation of this reform. 2. This set of regulatory reforms was reviewed by the Boards of the National Commission for the Pension System (CONSAR) and CNBV during 2015. 3. Changes to the FONADIN were executed in 2015 and will continue during 2016. The Federal Government is analyzing ways to optimize FONADIN's assets (51 toll highways) in order to leverage private investment in infrastructure.
	Status	• All measures are currently being implemented.
Impact of measure	• The Financial Reform will reduce costs and promote efficiencies in credit origination mainly for SMEs, and will provide a new mandate for Development Banks, in order to foster financial market development and financial inclusion. • The capital market regulations will help channel more effective institutional investors and commercial banks to infrastructure projects, fostering capital mobilization for this sector. • The FONADIN will foster private participation in infrastructure projects through PPPs.	

Other Non-key Commitments

• The policy action:	Telecom Reform
Implementation path and expected date of implementation	• The Telecom Reform was approved in 2013. By May 2014, following the passage of its secondary legislation, its implementation phase began. The proposed legal and regulatory framework is now in effect and is already showing signs of a significant impact.
Status of implementation and impact	• The Federal Communications Institute (IFT, for its acronym in Spanish), focuses on telecommunications and broadcasting. This agency continues to be fully operational. The IFT has exclusive authority for regulation and competition enforcement in the telecommunications and media industries, and has a range of new regulatory capabilities to promote competition, such as imposing obligations on dominant operators. • Regarding investment, the Telecom Reform now allows for 100% foreign direct investment (FDI) in telecommunications and up to 49% in broadcasting. Previously, the Federal Government prohibited FDI in broadcasting and limited to 49% FDI in the Telecom sector. Tangible results are already visible, as global companies have expressed their interest in entering the Mexican telecommunications sector. Since 2015, there are new players in the telecomm market: AT&T (investment size: 7.4 billion USD), Eutelsat (831 million USD) and Virgin Mobile (45 million USD). Through 2014 and early 2015, the Reform has already yielded positive results for users through lower prices and higher quality in communication services. Among these positive results are: − Extra charges in long-distance phone calls were eliminated, while other telephone and mobile services have registered lower prices than previous years. − Lower services prices and greater competition are already increasing broadband penetration. According to the Federal Telecommunications Institute, from December 2012 to December 2014, the level of penetration of wireless broadband doubled from 23.6 to 43 subscribers per 100 inhabitants. In addition, mobile broadband penetration has raised 57.5 million users, which represents a 409% increase in the fourth quarter 2012 with respect to third quarter of 2015. 54 million internet users, which represents an increase of 20% from the fourth quarter of 2012 to the fourth quarter of 2014. • During 2016, the Federal Government will continue working on the implementation of the Telecom Reform. − By the end of 2015, the transition from analogue to digital TV was completed.

• The policy action:	Unemployment Insurance
Implementation path and expected date of implementation	• The policy is still under discussion by Congress.
Status of implementation and impact	• Once the reform is approved, its progress could be verified by the number of applicants that are granted unemployment insurance in a given year.

Investment Strategy Commitments

	Facilitators	Safeguards
	Fiscal Responsibility Law for States and Municipalities. The Law was enacted in April, 2016. The main elements are: • Congress is empowered to issue fiscal responsibility laws in order to foster sound management of public finances in States and Municipalities. • The States' Constitutions will strengthen responsibilities for public officials in case of improper use of public resources. • Local governments should achieve a balance budget. • Congress can establish the general criteria for debt contracting by States and Municipalities. • States and Municipalities debt should be authorized by two thirds of local Congress. • States and Municipalities will be able to borrow resources for refinancing or restructuring existing obligations, and for productive projects. These	

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<tr><td></td><td>resources could not be used for current expenditure.
• States and Municipalities have the obligation to register and publish their debt and payment obligations in a Public Debt Record.
• Short-term liabilities should be paid at the latest three months before the local administration ends.
• The Superior Auditing Office of the Mexican Federal Government will be able to review states and municipalities' Federal Government guaranteed debt, as well as the use of these resources.</td><td></td></tr>
<tr><td>Infrastructure</td><td>Execution of the National Infrastructure Program.

The National Infrastructure Program, which includes more than 700 projects that account for more than 550 billion USD.

• Several projects are underway, including toll highways, roads, ports and energy projects.
• In addition, the construction of the New Airport of Mexico City is in progress, which is expected to start operating by 2020.</td><td>Develop new vehicles to foster institutional investors' participation in infrastructure financing.

New instruments were recently launched:

• FIBRA E, which is an instrument for cashing out mature infrastructure projects, including energy projects. This vehicle shares many characteristics with Master Limited Partnerships (MLPs). This instrument facilitates investment in infrastructure and energy sectors.
• Investment Projects Certificates (CerPIs), which emulates a typical private equity structure, allowing the participation of top global asset managers and local and international institutional investors.
• Educational Infrastructure Certificates, which will be traded through the Mexican Stock Exchange.</td></tr>
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SMEs	**Implement the Youth Credit Program, which facilitates access to credit for entrepreneurs under the age of 30.** In February 2015 the Federal Government launched the Youth Credit Program, through which NAFIN, the major National Development Bank for SME financing, will provide credits to entrepreneurs between 18 and 30 years old who want to start a business or expand the ones they have already.	**Reduce informality through the "Growth Together Program" (Programa Crezcamos Juntos), the benefits of which include tax exceptions, housing loans, inclusion to health and social security programs and financing for SMEs.** The Federal Government created the Growth Together Program through which different Government agencies linked their programs in order to foster formality. To be registered in this program, enterprises must fulfil their obligations relating to the payment of taxes. The program provides different tax exceptions for the first ten years; a 50% discount in health and social security fees; and, housing loans and consumer credits for employees. Likewise, by registering in this program, SMEs are able to access bank financing to increase their productive capacity.

Annex 2. New and Adjusted Policy Commitments since Antalya

<table>
<tr><th>• The new or adjusted policy action:</th><th>Increase productivity, boost employment and create wealth in less developed regions through the creation of Special Economic Zones</th></tr>
<tr><td>Implementation path and expected date of implementation</td><td>The approved Law regarding Special Economic Zones includes: (1) provision of fiscal, commercial, financial benefits, jointly with specific regulation and the development of economic infrastructure; (2) the government will provide flexibility in each zone to establish specific incentives regarding customs regime, tariff policy and merchandise control, depending on their initial conditions and the productive orientation of the region; (3) to ensure procedure efficiency and to cut red tape, there will be coordination and cooperation among the three levels of government to facilitate the establishment and operation of new enterprises and (4), Special Economic Zones will guarantee high standards in transparency and accountability.
Special Economic Zones aim to democratize productivity at the regional level, for these zones (located in the southern states) to have the same opportunities for development and welfare as the rest of the country. The general objective is to develop regional value chains, expand local public services and provide benefits for both Special Economic Zones' populations and neighboring communities. The medium and long-term goal is to trigger productivity of the southern region and to establish structural conditions that will generate more wealth and opportunities for integral development.
These industrial zones will spearhead a fundamental change in the production structure of the regions, raising the presence of high-productivity economic activities.
In May 2016, the President decreed the creation of the first Special Economic Zones and enacted the Federal Law on Special Economic Zones, which concluded the legislative stage and marked the start of the implementation phase. The regulation was published in June, so that the Special Economic Zones would be in place by the end of the year. The Law included the creation of the Federal Administration for the Development of Special Economic Zones, a decentralized agency of the Ministry of Finance, in charge of the implementation phase of the SEZ. This body now has regulation, planning and promotion functions of the SEZ in accordance with the best international practices. The head of this agency was also named in June.

The Special Economic Zones initiative is already under implementation.
On September 29, 2015, the President of Mexico sent the Initiative for the Federal Special Economic Zones Act to Congress.
On September 30, 2015, the Initiative was referred to the Economic, and Budget and Public Accounts Committees for an opinion.</td></tr>
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	• On December 14, 2015, the Chamber of Representatives approved the document and issued the Law with changes in 28 articles, adding 3 new ones to the 47 articles proposed by the President of Mexico. • On December 15, 2015, it was referred to the Joint Committee on Finance and Public Credit; Trade and Industrial Development, Population and Development; and Legislative Studies for examination; with the opinion of the Southern Border Affairs; Special South-Southeast and Special Productivity Committees of the Senate. • On April 14, 2016, the Senate approved the initiative amending the Act. • On April 27, 2016, the Chamber of Representatives approved the changes made by the Senate. • **Federal Law Special Economic Zones** The bill creates for the first time the legal concept of Special Economic Zones and sets the policy framework for the development of these areas in a comprehensive and orderly manner. The project is structured to provide flexibility and establish a tailor-made stimulus package for each zone to be developed. Also, it empowers the offices of the Federal Public Administration to establish special programs and public policies. Special Economic Zones can be created from decrees issued by the President of Mexico, and companies established within the perimeter will enjoy the benefits set out in those decrees. The first three zones are Lázaro Cárdenas (in the state of Michoacán), Puerto Chiapas (in Mexico's southernmost state of Chiapas), and the Isthmus of Tehuantepec (across several southern states in Mexico). Also, the government has plans to create a zone in the "Oil-belt states" of Tabasco and Campeche for 2017. Each zone will have a Master Plan, with elements and general characteristics of infrastructure and services adapted to the resources and needs of every particular area, which will be reviewed and adjusted every 5 years. The deadlines for the implementation stage of these projects are as follows: • In January 2017, the design and approval of the institutional legal framework is to be completed. • By March 2017, the approval of development programs by the Interministerial Commission and the signing of coordination agreements with states and municipalities will take place. • By June 2017, the declaratory, licensing and assignments should be in place. • In October 2017, the construction and operation of the Zones will begin. • By September 2018, an anchor tenant, for instance, an industrial company that can attract suppliers and others, should be in place for each zone.

What indicator(s) will be used to measure progress?	Economic growth in the Special Economic Zones.
Explanation of additionality or adjustment (where relevant)	http://www.presidencia.gob.mx/zonaseconomicasespeciales/

• The new or adjusted policy action:	**Improving the rule of law to lift potential growth by strengthening the legal framework to realize the reforms' full potential**
Implementation path and expected date of implementation	Mexico's efforts to improve the rule of law will help realize the full potential of the structural reform agenda. In this regard, the government has taken the necessary actions by approving two reforms to strengthen the Mexican legal framework. The first reform is the National Criminal Procedure Code and the second one refers to the New Appeal Law. First, the National Criminal Procedure Code reform unifies the criminal justice model which allows our system to transition towards a model shared by the Federation and the states, in order to (1) facilitate coordination between authorities; (2) increase investigation effectiveness at the federal and local levels; (3) provide greater legal certainty regarding the decisions of judges and courts; and (4) prevent the diversity of rules from creating scope for impunity. This code includes a new system of oral adversarial criminal justice, the implementation of which, according to the Constitution, was completed in June 2016. The new Justice System enacted in the reform has already been implemented at a federal level in all of the 32 states. The first stage began in November 2014 with the implementation in 2 states. The second and the third stages were implemented in March 2015 and August 2015, respectively, adding 6 more states in total. In November 2015, 7 more states started the operation of the new system. In February 2016, the fifth stage included 9 more states, while the sixth, scheduled in April 2016, added four states. The seventh and the last stage of nationwide implementation began on June 14, 2016 with the last 4 states to achieve a full operation status. In this way, the reform is fully implemented. Second, the Reform will expand the protection provided to citizens' rights, in order to make the administration of justice more expeditious and effective; to simplify and to modernize the legal process, and to strengthen the Judicial Branch of the Federation. The Injunction Law Reform has three main axes: (1) it expands the sphere of the protection of rights (i.e. human rights provided for in international treaties will receive direct protection); (2) the effectiveness of Mexican justice increases (i.e. filing for an injunction may now be done online using the Electronic Signature); and (3) it strengthens the Judicial Power of the Federation, particularly the Supreme Court of Justice (i.e. the Court is empowered to remove from office and report to the District Judge both the authority responsible and their immediate superior when he/she fails to comply with an injunction sentence). This reform has also been fully implemented and resulted in several cases in the protection of citizens' rights. It is important to mention that in the process of designing the aforementioned reform, the government included the participation and proposals from the civil society, renowned scholars and justice experts. A recognized academic institution, CIDE, organized consultation forums on Justice, in which over 400 experts participated in an open and plural exercise. The results were concrete recommendations to strengthen the

	rule of law, enforce the rights of individuals, and the timely and efficient resolution of conflicts. The government acknowledged that everyday justice needed a reform in order to be equal, faster and simpler, so that all Mexicans can access justice and be satisfied with the results.
What indicator(s) will be used to measure progress?	Number of states that have the new justice system fully implemented. The National Survey on Criminal Justice System (ENSIJUP) aims to establish the methodology and the baseline to be able to measure the impact that the process of implementing the Penal Reform has had on society. The study is divided into three major categories: i) a survey with the perception of society on the Criminal Justice System; ii) a focus groups made up by operators; and iii) a cross-check analysis of quantitative and qualitative results.
Explanation of additionality or adjustment (where relevant)	http://www.setec.gob.mx/ http://www.setec.gob.mx/es/SETEC/Mapa_de_Gradualidad http://reformas.gob.mx/en/appeal-law/what-is

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- The new or adjusted policy action:

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<th>Implementation of a multi-year public spending adjustment plan to secure fiscal sustainability and preserve macroeconomic stability in the current adverse environment.</th>
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<td>Implementation path and expected date of implementation</td>
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In the current adverse environment, the objective is to preserve macroeconomic stability by acting responsibly and with long-term fiscal health. As a result, the Federal Government is currently implementing a multi-year public spending adjustment measure. This adjustment aims to preserve the path of public finances, in order to achieve the fiscal consolidation path, in a context of volatility, widespread appreciation of the dollar and lower oil prices. With this strategy, we are establishing conditions for a timely reduction in public spending to ensure an orderly decline in financing requirements for upcoming years.

On the fiscal front, the government maintains fiscal discipline, responsible management of public debt and an oil hedging strategy to keep sound public finances and preserve macroeconomic stability.

The financial reform has already paid off allowing to partially offset a real reduction in oil revenues of the Federal Government, without considering the benefits associated with oil hedges or the operating surplus from the central bank. Hence, in order to face the external environment and its effect on public finances, the government has taken action.

1. Through 2016, the Federal Government implemented several measures:

- The General Economic Policy Preliminary Guidelines document for 2016 is based on realistic premises, considering an adverse external environment, and foresees the accomplishment of the public finances objectives of the Economic Program for 2016.
    - It mentions the need of a fiscal adjustment of 176.4 billion pesos for 2016, which represents 0.9% of GDP.
    - On February 17, the Federal Government announced an additional pre-emptive fiscal adjustment for 2016 that amounts to 132.3 billion pesos, about 0.7% of GDP. The pre-emptive adjustment consists of a reduction in Federal Government spending for 2016 by 32.3 billion pesos and a 100 billion pesos adjustment in Pemex current fiscal year budget. The adjustment of the Federal Government agencies was focused on current expenditure, which accounts for 60% of the total.
    - On April 11, Banco de México announced the delivery of 239 billion pesos to the Federal Government on account of their operating surplus, corresponding to the 2015 fiscal year. In accordance with the Federal Budget and Fiscal Responsibility Law, these resources will be used to reduce debt and improve the financial position of the Federal Government.
        - 70% of the total amount, equivalent to 167 billion pesos, will be used to repurchase Federal Government debt and to reduce the issuance of Federal Government debt during 2016. Of the

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	remaining 30% (71.7 billion), 70 billion pesos will be deposited into the Budgetary Revenues Stabilization Fund (FEIP); and approximately 1.7 billion will be used to pay pending contributions to international organizations. This constitutes a capital investment for the Federal Government. o The receipt of the operating surplus will be reflected in an improvement of the Public Sector Borrowing Requirements (PSBR) and the Historical Balance of the Public Sector Borrowing Requirements (HBPSBR). • On June 24, in order to strengthen the macroeconomic position of the country in response to possible consequences of the United Kingdom leaving the European Union, the Ministry of Finance announced a second fiscal pre-emptive adjustment to programmable expenditure, exclusively within the Federal Government of Ps. 31.7 billion. Of which 91.7% corresponds to current expenditure and affected neither social program beneficiaries nor the national security budget. 2. For 2017: • To comply with the fiscal consolidation path in 2017, the Government foresees an adjustment of programmable expenditure, excluding high economic and social impact investment, for 175.1 billion pesos. • Following the adjustments mentioned before, it is estimated that the Historical Balance of the Public Sector Borrowing Requirements (HBPSBR) will initiate a downward trend in 2017, one year ahead of schedule, consistent with the fiscal consolidation effort in place. • The Federal Government will submit a budget proposal for this year that considers all previous adjustments and efforts of the Government to keep sound public finances. Thus, the commitment not to raise taxes or increase indebtedness is upheld. • Additionally, it is expected to return to a budget balance target of 0% of GDP in the broadest measure of deficit, without considering high economic and social impact investment.
What indicator(s) will be used to measure progress?	Comply with the fiscal balance trajectory published in the Economic Policy Guidelines for 2016.
Explanation of additionality or adjustment (where relevant)	http://finanzaspublicas.hacienda.gob.mx/work/models/Finanzas_Publicas/docs/ori/Ingles/Other/2016/Press_Release_Preemptive_Fiscal_Adjustment_Announcement_160218.pdf http://finanzaspublicas.hacienda.gob.mx/work/models/Finanzas_Publicas/docs/ori/Ingles/Other/2016/Press_Release_BANXICO_160413_2055.pdf http://finanzaspublicas.hacienda.gob.mx/work/models/Finanzas_Publicas/docs/paquete_economico/precgpe/precgpe_2017.pdf

Annex 3. Past Commitment – St. Petersburg fiscal Commitment

Estimate Projections

	2014-15*	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21
Gross Debt							
ppt change							
Net Debt	47.6	50.5	50.2	49.9	49.6	49.2	48.5
ppt change	0.7	2.7	2.4	2.5	2.6	2.6	2.2
Deficit	-3.5	-2.9	-2.5	-2.0	-2.0	-2.0	-2.0
ppt change	0.0	-0.1	0.0	0.0	0.0	0.0	0.0
Primary Balance	-1.3	-0.4	0.2	0.9	1.1	1.2	1.2
ppt change	0.0	-0.2	0.1	0.0	0.0	0.0	0.0
CAPB							
ppt change							

* Figures can be presented on a fiscal year basis, should they be unavailable for the calendar year.

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

Estimate Projections

	2014-15*	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21
Real GDP growth [a]	2.5	2.4	2.6	3.0	3.0	3.0	3.0
ppt change	0.3	-0.5	-1.0	0.0	0.0	0.0	0.0
Nominal GDP growth	5.0	5.8	6.0	6.3	6.3	6.3	6.3
ppt change						0.0	0.0

* Figures can be presented on a fiscal year basis, should they be unavailable for the calendar year.

[a] It refers to the growth scenario used for public finances estimates.

Annex 4. Pre-Brisbane Commitments

Pre-Brisbane Commitments

Education Reform	
Structural reform	**Action Plan** *St. Petersburg*
Rationale for carrying forward	• One of the most powerful tools to promote inclusive growth is to ensure that all Mexican families have access to a quality education and have the opportunity to improve their educational outcomes.
Update on progress	• Since its implementation in 2013, the Education Reform has had the following results: - The National Evaluation System, the Professional Teaching Service and the Education Information and Management System were created and have become fully operational. - A comprehensive census of schools, teachers and students from primary and special education schools in Mexico was completed in 2014. Through this, the gaps, challenges and problems of almost 240 thousand schools, 24 million students and 1.8 million education workers were identified. - The program “Escuelas Dignas” was implemented, which aims to bolster school infrastructure, and has benefited 11 thousand schools, with a budget of 8 billion pesos in two years. - To strengthen self-management and take into account local needs, the Education Reform assigns more resources to school boards so that parents, administrators and teachers have a greater say in the management of their schools. In the first phase, 7 billion pesos were granted to 20 thousand schools. - Full-time schools have increased from 6 thousand to 23 thousand in the last two years; over half of them provide free school lunches, benefiting low-income students. - A Professional Development Program for Teachers was instrumented, which provides training and skills building. - The old school performance tests, ENLACE and EXCALE, were substituted by the National Learning Assessment Plan (PLANEA), designed by the new autonomous National Institute for Educational Evaluation.

Labor Reform	
Structural reform	**Action Plan** *St. Petersburg*
Rationale for carrying forward	• It responds to the demands of workers and employers, as well as a society concerned with creating more jobs and more humane working conditions; particularly to enable young people, women and older adults to join the work force. • It guarantees more rights for vulnerable groups. • It grants greater powers to the labor authorities to provide greater protection and security for workers and the workplaces themselves, and even imposes exemplary sanctions for non-compliance with work regulations. • It contributes to achieving a prompt, expeditious administration of justice, to provide the boards of conciliation and arbitration with more and better tools. • It brings labor standards into line with the decisions of the Supreme Court of Justice. • It implements the commitments embodied in various international instruments, Mexico has signed regarding the workplace.
Update on progress	The following changes were introduced and are fully implemented: • New forms of contracts are established: probationary and training, which facilitate access to the labor market by making it more flexible. • Subcontracting or outsourcing will also be regulated to prevent abuse of this measure. • The calculation of overdue wages for unfair dismissal has been modified. 100 percent will only be paid for the first year, after which 2% compounded interest will be incurred. • The figure of the "blind promotion ladder," according to which the most senior rather than the most skilled worker and/or productive worker filled vacant posts, has been eliminated. • The exclusion clause due to separation from collective labor contracts has been eliminated to prevent a worker who resigns from a union from losing his job as a result has been eliminated. • Free, secret voting in elections of trade union leaders has been established together with the right of unionized workers to demand information and accountability. • Information related to trade union and collective bargaining agreements is regarded as public.

	• Labor authorities are entitled to restrict access to a workplace in the event of imminent danger. • Penalties for non-compliance with labor standards have been increased. • Protection of substantive equality between male and female workers has been established. • Better protection has been provided for workers in various aspects and situations such as the following: bullying and harassment, pregnancy, breastfeeding, parenting, disability and activities such as child labor, domestic, farm and coal mine workers. • Child labor outside the family circle has been criminalized and is punishable under the law. • Professional career service on the boards of conciliation and arbitration has been established, procedures have been streamlined and a new, most expeditious procedure for social security trials has been created. • As a result of the reform, formal employment is growing considerably faster than GDP. During 2014 and the first half of 2015, formal employment grew by 4.3% and 4.5%, formal employment also grew by 634,153 job positions(+3.6%) from April 2015 to the same period in 2016, while GDP growth was 2.2% and 2.4%, respectively.

Annex 5. Key Economic Indicators

Please update table of key indicators as follows:

Key Indicators

	2015***	2016	2017	2018	2019	2020
I. Macroeconomic Indicators						
Real GDP (% yoy)	2.5	2.4	2.6	3.0	3.0	3.0
Nominal GDP (% yoy)	5.0	5.8	6.0	6.3	6.3	6.3
Output Gap (% of GDP)*	-0.7	-0.4	-0.2	-0.1	0.1	0.2
Inflation (%, yoy)	2.1	3.2	3.0	3.0	3.0	3.0
Fiscal Balance (% of GDP)**	-1.1	-0.5	0.0	0.0	0.0	0.0
Unemployment (%)	4.4	4.0	3.9	3.6	3.5	3.5
Savings (% of GDP)	22.4	21.8	21.9	22.1	22.3	22.6
Investment (% of GDP)	22.4	21.8	21.9	22.1.3	22.3	22.6
Public Fixed Capital Investment (% GDP)	3.7	3.6	3.4	3.3	3.2	3.2
Private Fixed Capital Investment (% GDP)	18.2	18.2	18.4	18.7	19.0	19.3
Total Fixed Capital Investment (% GDP)	21.9	21.8	21.8	22.0	22.2	22.5
Current Account Balance (% of GDP)	2.8	3.2	3.0	2.9	2.8	2.7

[a] **It refers to the growth scenario used for public finances estimates.**

***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.**