



Market Commentary  
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Insigneo Weekly Dispatch

# Walking on a Mexican Tightrope

Our thoughts on the first days of Sheinbaum's presidency and what we can expect as market participants.

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**Melissa Ochoa Cárdenas**

Investment Strategist

Insigneo

## Walking on a Mexican Tightrope

On October 1, Claudia Sheinbaum was sworn in as Mexico's first female president. Seen by many as ex-president AMLO's protégée, Sheinbaum came to power with the support of the ruling party, Morena, and with the daunting task of bringing to fruition several of the former president's previous plans while keeping Mexico on the path of progress and development. With the first two weeks of her six-year period coming to a close, we deemed it fit to review her initial moves, Sheinbaum's take on the implementation of the recently approved reforms already taking place, and how this may look for investors and market participants alike.

The start of Sheinbaum's presidency occurred amid controversies caused by the approval of the judicial reform that, aside from allowing for the popular election of judges across Mexico's judiciary branch, raised concerns about the country's fiscal stability and its capacity to do business with international counterparties in the near future. Since then, additional reforms have taken shape and started their way through the Mexican Congress, with the energy reform taking center stage. This reform, approved on October 9, aims to reassert the state-owned enterprises - SOEs, such as Comisión Federal de Electricidad - CFE - and Pemex, as public companies. According to market analysts, this move seems to leave both former SOEs better positioned than private companies. Furthermore, according to Sheinbaum, this reform hopes that CFE and Pemex stop competing with the private

sector pursuing profitability, and instead, should be governed by public law.

Additionally, this reform implies a reversal of the 2013 reform presented by former President Enrique Peña Nieto, as well as a refocus of the two companies that now should aim to prioritize government policies over their profitability. This situation could limit the involvement of private investment in the Mexican energy sector, further complicating private investment and exerting pressure on the country's public finances.

Meanwhile, the energy reform is raising concerns surrounding the upcoming USMCA renegotiation, as well as Mexico's ability to attract foreign investment in the renewable energy sector. The latter is crucial against the backdrop of the Sheinbaum administration, which is focused on achieving the milestone of Mexico's renewable energy reaching 45% by 2030. This objective can only be attained with the help of private capital, especially if we consider that according to market experts, Sheinbaum's energy plan could cost up to USD 50bn. Against this backdrop, Alicia Bárcena, Sheinbaum's Secretary of the Environment and Natural Resources, stated that the administration would review the rules of public-private partnerships to eliminate what were considered unfair advantages.

Even if the energy reform is seen as a potential headwind to the industry, there are some dissenting voices in the market. Recently, Fitch Ratings stated that the reclassification of Pemex could have a positive impact on its credit rating since this would imply a tighter relationship between the

government and the company; however, Fitch stated that its base-case scenario is one where even if the reclassification takes place, the government does not guarantee Pemex's debt. This scenario would imply an improvement in Pemex's credit rating from 'B+' to 'BB.' Furthermore, if the Mexican government concedes a partial guarantee of Pemex's debt, Fitch considers that the company's credit rating could be upgraded to 'BBB-', bringing Pemex back into investment grade territory. The positive news seems to have been penciled in by Pemex's 5-year CDS, which exhibits a ~23bps tightening since the beginning of the Sheinbaum administration.

It is worth keeping in mind that Sheinbaum's administration is aware of the importance of international partnerships for Mexico to continue growing, which is why her cabinet has made key efforts in attracting foreign direct investment and in keeping an open, fluent relationship with international counterparties. As such, Economy Secretary Marcelo Ebrard stated in a summit with some key players in the Mexican private sector that they are a priority within the Sheinbaum administration.

Focusing on the macroeconomic backdrop, it has been highlighted in several stances that Sheinbaum is inheriting a daunting fiscal situation which, according to the Economist Intelligence Unit, includes the widest deficit since the 1980s amid slowing growth and weak revenue-raising capacity. Therefore, the Sheinbaum administration will find itself in a complicated position to implement some of its campaign promises that entail social benefits and will most probably force it to implement

spending cuts. This fiscal picture will take the spotlight once the 2025 budget proposal is presented in November.

This challenging perspective contrasts with a rosier picture presented by the latest government figures, which include a GDP forecast of 2.5 – 3.5% for 2024 and 2 – 3% in 2025 – a stark contrast from the 1.5% projected GDP growth that analysts surveyed by Bloomberg forecast. Furthermore, economic growth can also be affected by a potentially less favorable investment climate due to the judicial reform, which has already weighed on the MXN: since its approval, the MXN has depreciated more than 3%, and year-to-date, becoming the second most-depreciated currency in Latin America.

In sum, it seems like Sheinbaum will be walking on a tightrope in the initial part of her administration: aside from having to face a challenging fiscal

picture with minimal room for maneuver, any potential decisions that lead to her deterring from her campaign proposals will likely trigger a backlash from Morena which could, in turn, set off clamors from party members to radicalize Sheinbaum's cabinet. Thus, Sheinbaum's stance will have to be that of a mediator who can reach the right mix between favoring AMLO's legacy and bringing Mexico back to the path of sustained growth propelled by investment and not by government spending.



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