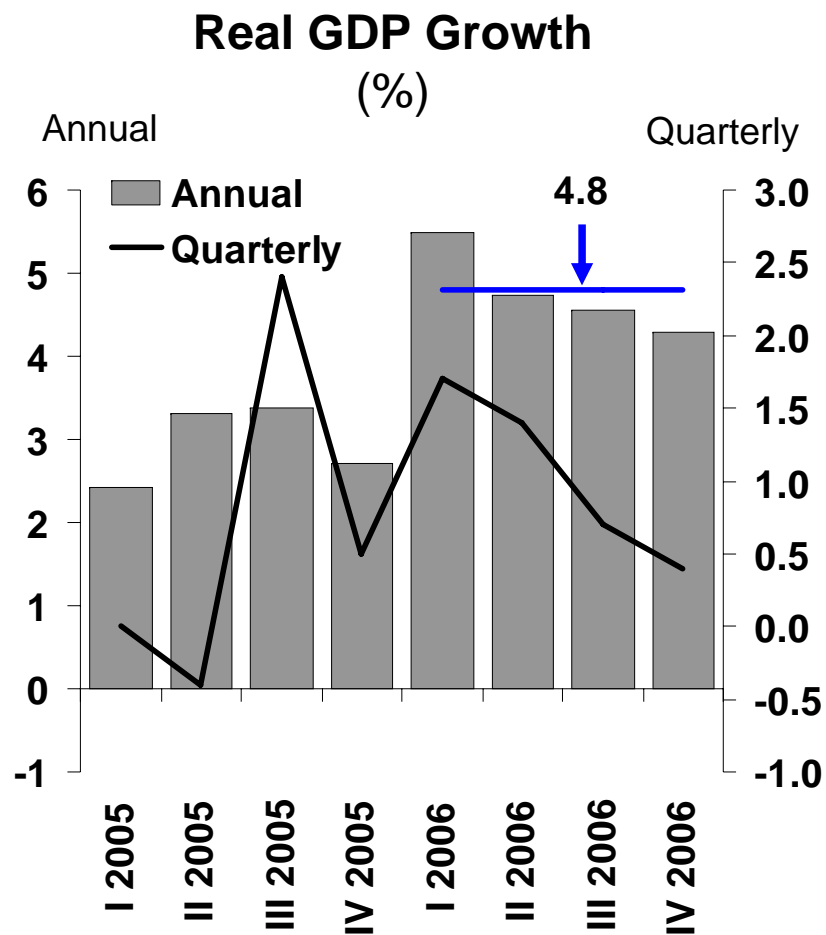




The Mexican Economy: 2006 - 2007

March 28th 2007

In 2006, the Mexican Economy grew 4.8% in real terms. This growth reflected the dynamism of all sectors in the economy.



Source: INEGI.

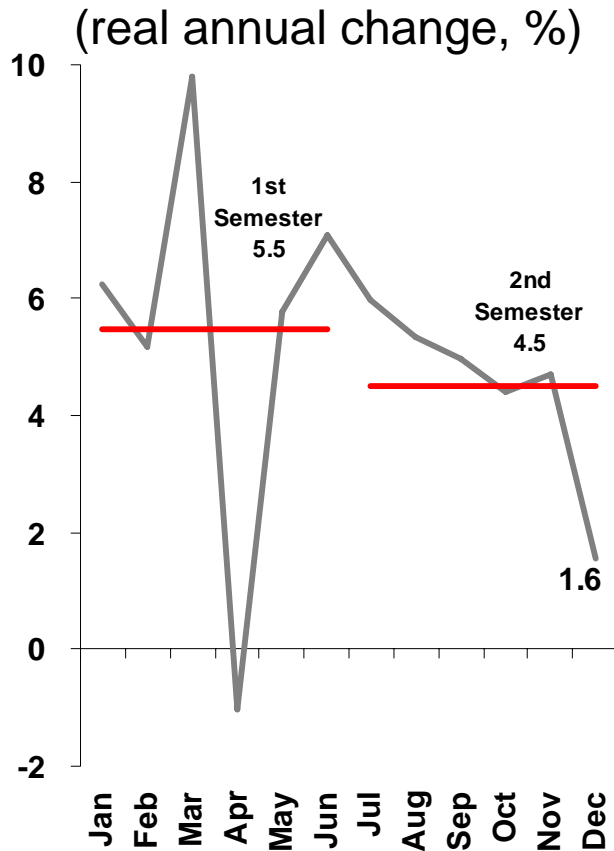
Real GDP Growth (annual variation, %)					
	2006				2006
	I	II	III	IV	
GDP	5.5	4.9	4.5	4.3	4.8
Agriculture	2.7	8.0	-2.3	9.8	4.8
Industrial	7.1	3.9	5.4	3.6	5.0
Services	5.4	5.3	4.7	4.2	4.9

Aggregate Demand and Supply (annual variation, %)					
	2006				2006
	I	II	III	IV	
Supply	8.4	7.2	7.1	5.3	7.0
GDP	5.5	4.9	4.5	4.3	4.8
Imports	16.0	12.9	13.2	7.6	12.4
Demand	8.4	7.2	7.1	5.3	7.0
Total Consumption	6.5	5.8	5.2	3.1	5.1
Investment	13.0	9.7	10.1	7.4	10.1
Exports	13.8	10.7	11.1	9.3	11.2

Source: INEGI.

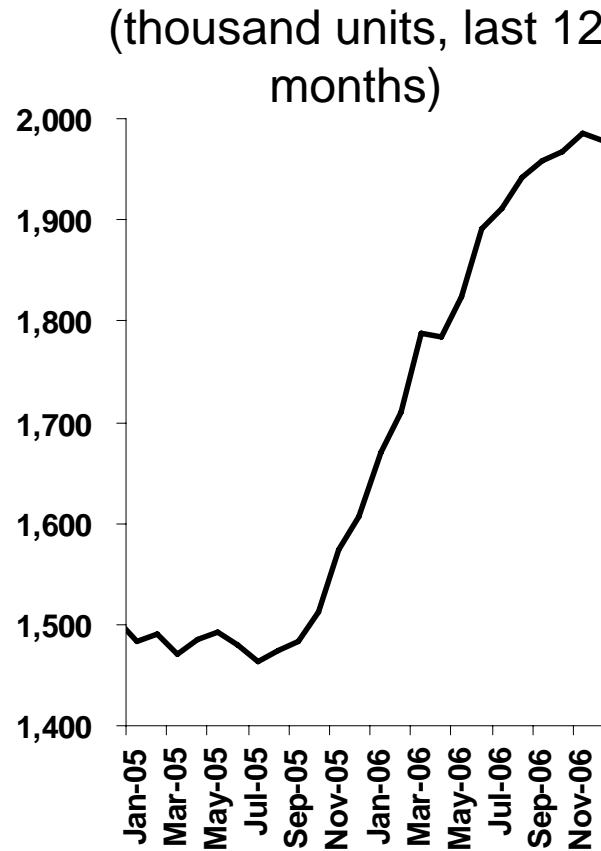
However, industrial production decelerated in the second half of 2006. This is explained mainly by the deceleration of industrial production in the US and the behavior of the automotive sector in Mexico. This was reflected in lower export growth at the end of 2006.

Industrial Production in 2006



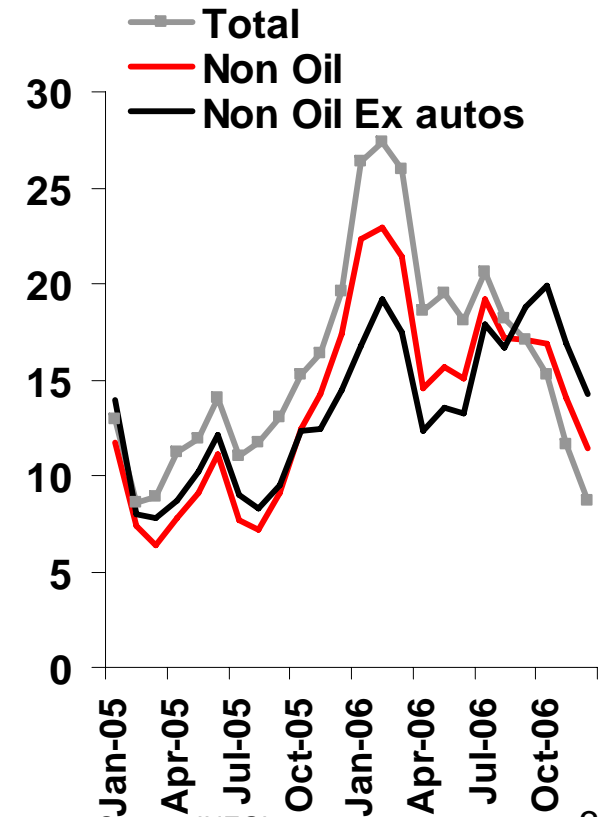
Source: INEGI.

Automotive Production in Mexico



Source: AMIA.

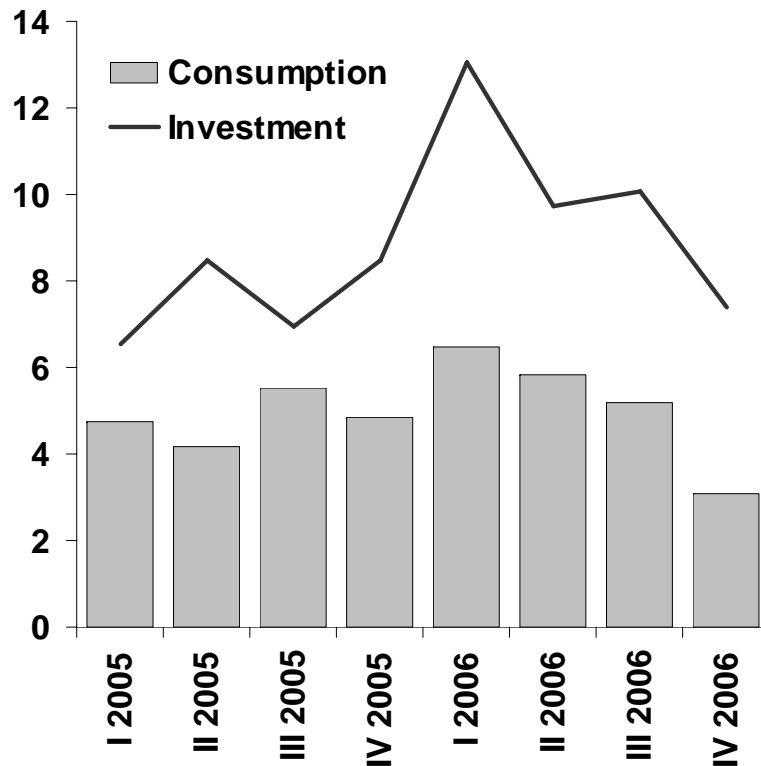
Exports
(real annual change, %, 3m mov. avg.)



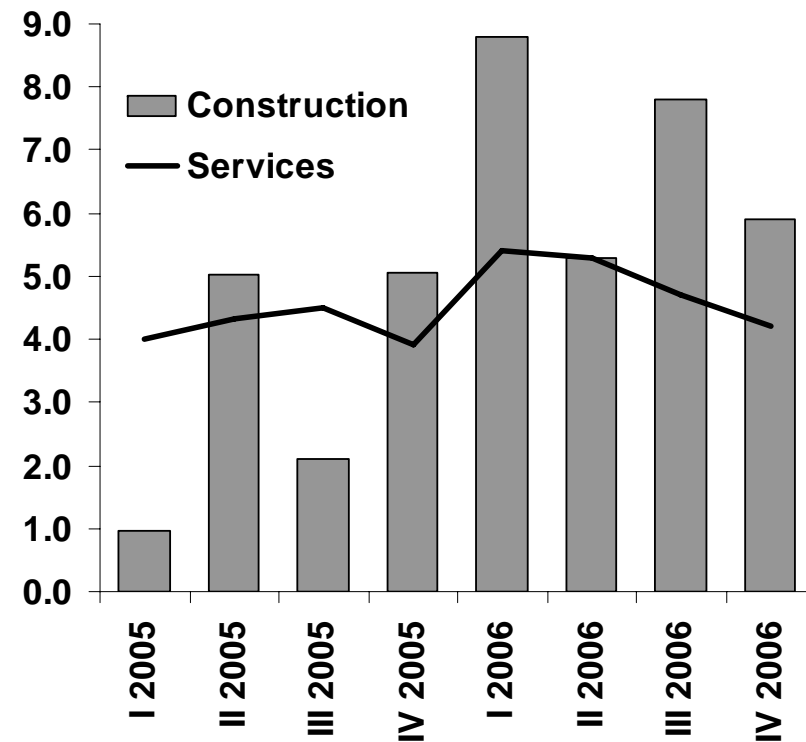
Source: INEGI.

Domestic demand grew at high annual rates, translating into high and stable growth of the construction and service sectors.

Consumption and Investment
(Real annual change, %)



Construction and Services
(Real annual change, %)



*/ Data for the fourth quarter of 2006 is the annual growth of the October-November period. Source: INEGI.

Source: INEGI.

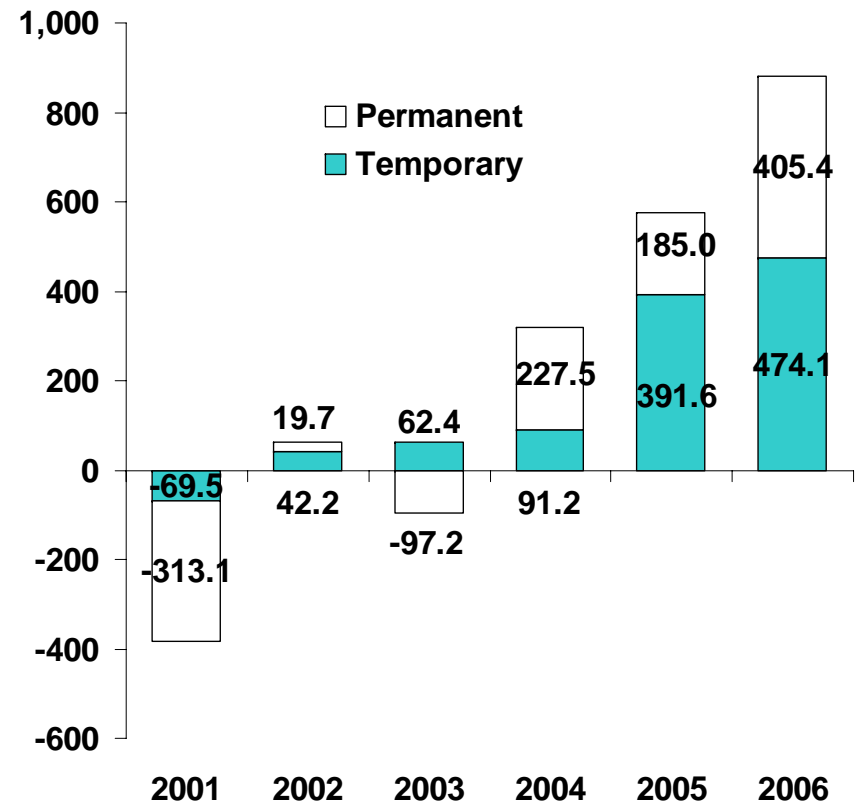
During 2006, the number of workers affiliated to IMSS increased by 880,000 for an annual growth rate of 6.7%. This was the highest annual increase on record.

Workers Affiliated to IMSS
(annual change, %)



Source: IMSS.

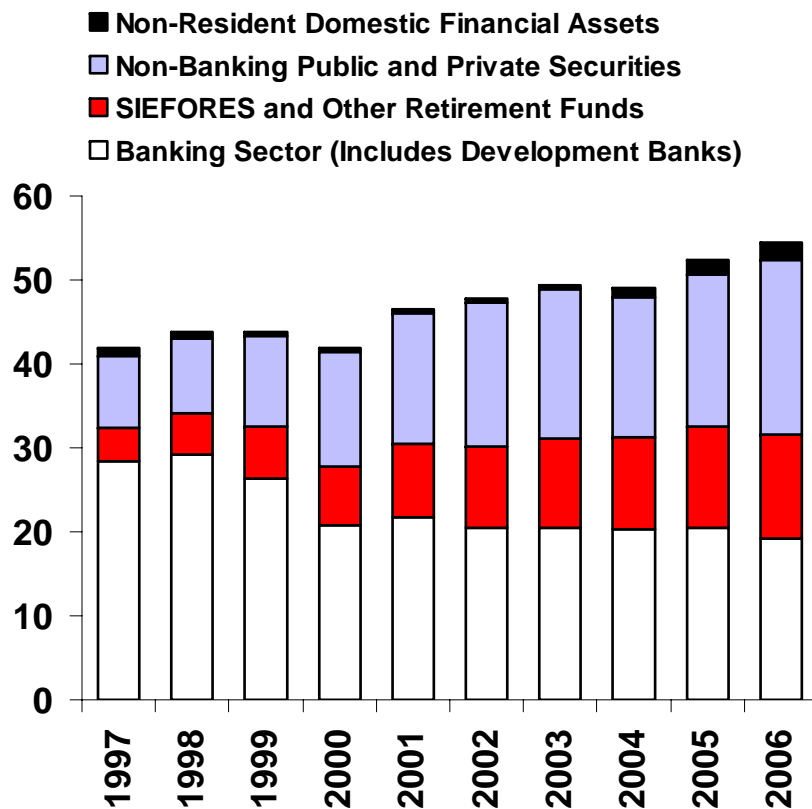
Formal Jobs Created
(annual change, thousands of workers)



Source: IMSS.

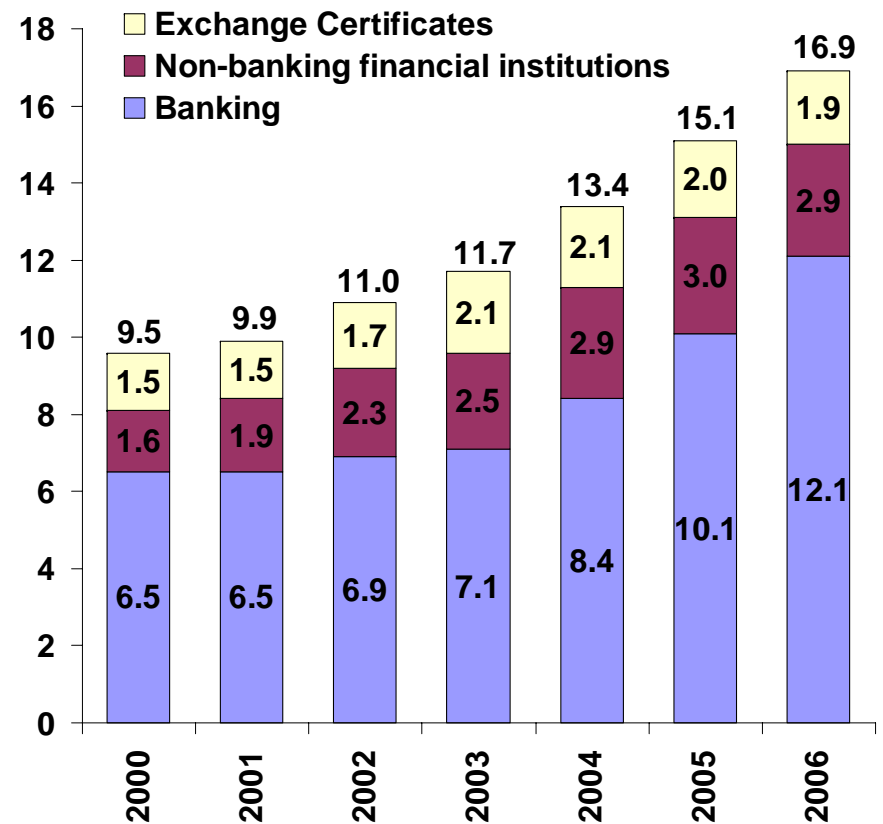
Macroeconomic stability promoted higher financial savings and credit to the private sector. The latter grew from 15.1% of GDP in 2005 to 16.9% in 2006, an increase of 297 billion pesos.

Financial Savings
(% of GDP)



Source: Banxico

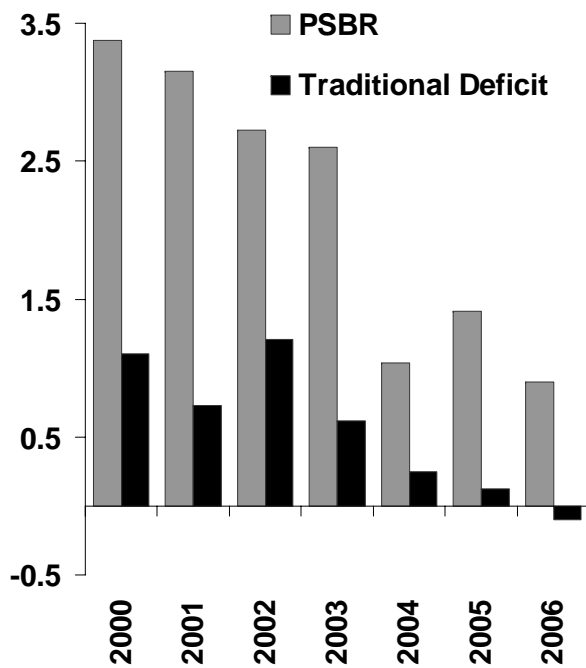
Credit to the Private Sector
(% of GDP)



Source: Banxico and CNBV.

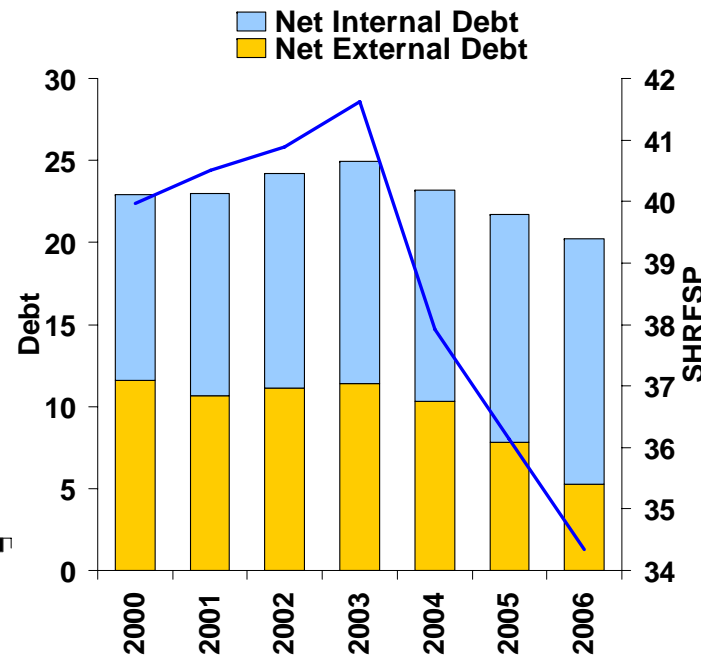
In 2006, the government's surplus and public debt were 0.23% and 20.3% of GDP, respectively. Additionally, the public sector continued substituting external for internal debt. The former posted a level of only 5.3% of GDP in 2006.

Public Deficit and Public Sector Borrowing Requirements (% of GDP)



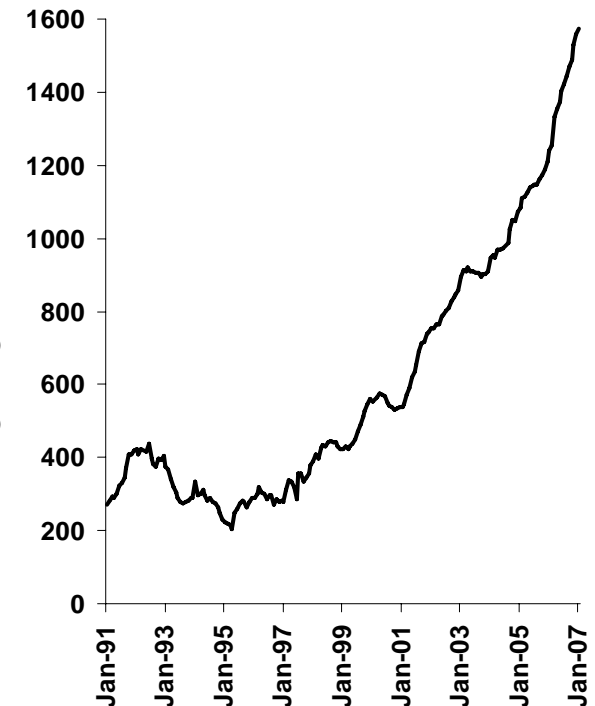
Source: SHCP.

Net Public Debt and Historical Balance of the PSBR (% of GDP)



Source : SHCP.

Internal Public Debt Maturity (days)



Source : SHCP.

Macroeconomic Outlook 2007

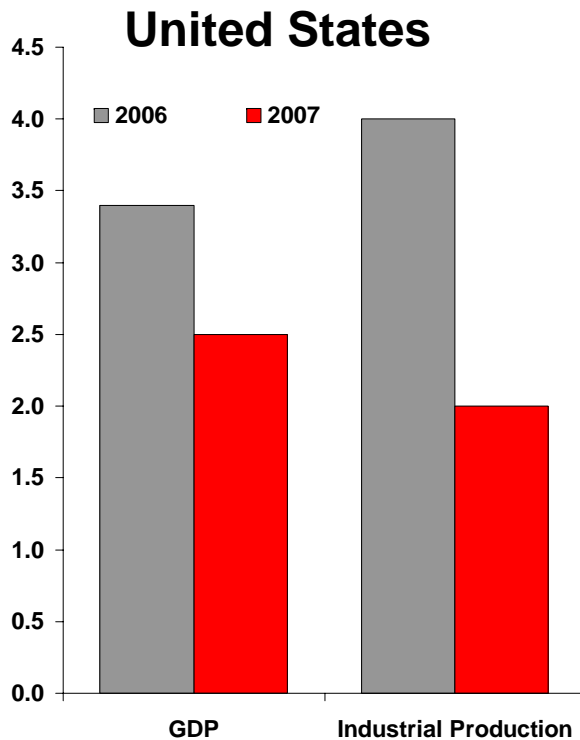
	2007	
	Projected	Expected by the Private Sector ^{1/}
Gross Domestic Product (real annual change)	3.6	3.5
Inflation (Dec/Dec)	3.0	3.6
Interest Rates		
28-day Cetes (% nominal average)	6.9	6.9
28-day Cetes (% real average)	3.9	-
Public Balance (% of GDP)	0.0	-0.2
Crude Oil Price (dollars per barrel)	42.8	45.4
Current Account Deficit (% of GDP)	-2.3	-1.0
Oil Production Platform (thousand barrels per day)	3,241.1	-
Oil Export Platform (thousand barrels per day)	1,648.0	-

*/ Economic Program for 2006 approved by Congress.

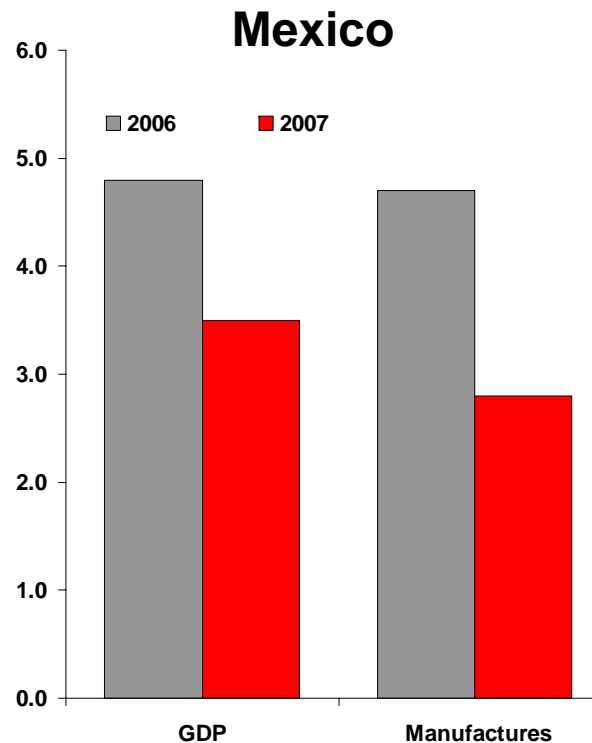
1/ Source: Encuesta Sobre las expectativas de los especialistas en economía del sector privado, February 2007, Banxico.

Compared with 2006, a deceleration is expected for the US economy in 2007 due to a decrease in the growth rate of industrial production. This will be reflected in lower growth in the Mexican economy. However, the Mexican economy has become less sensitive to the US business cycle.

Expected GDP and Industrial Production Growth
(annual change, %)

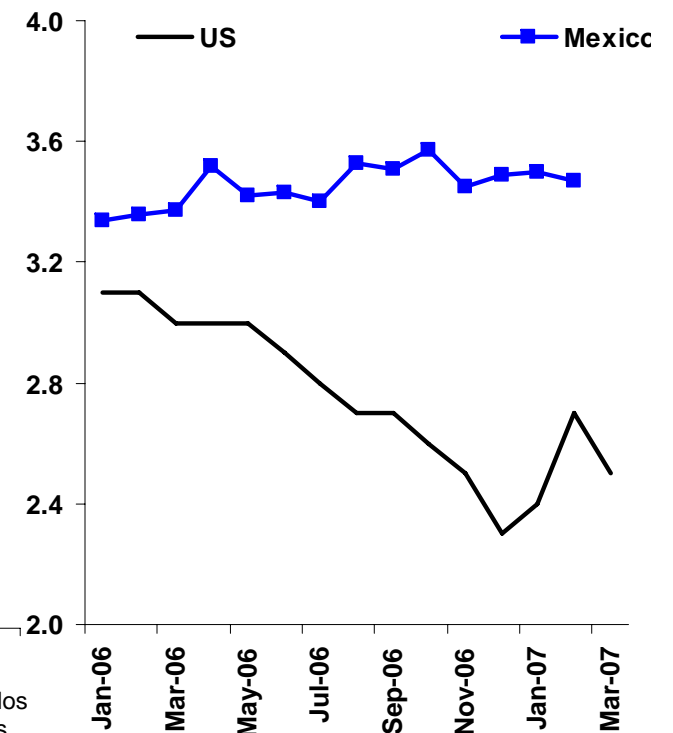


Source: Blue Chip Economic Indicators, March 2007.



Sources: INEGI, Encuesta Sobre las Expectativas de los Especialistas en Economía del Sector Privado, various months, Banxico; Latin American Consensus Forecast, March 2007.

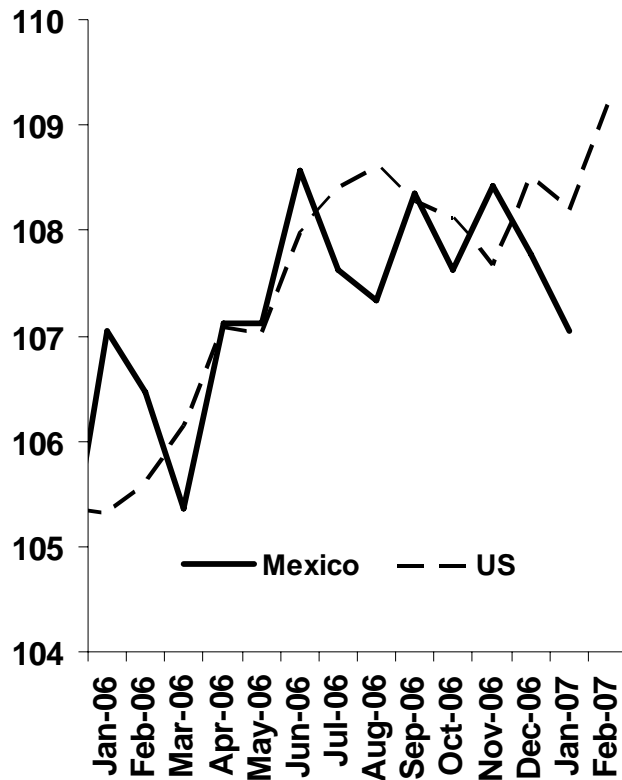
Expected GDP Growth for 2007
(real annual change, %)



Source: Banxico and Consensus Forecast

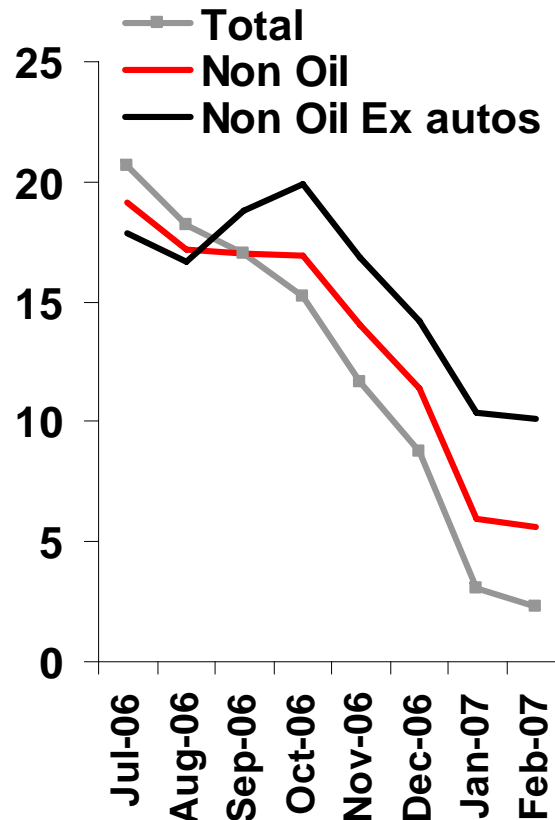
Slower growth in the United States has translated into a more moderate expansion of industrial production and exports in Mexico. In addition, in January there was a temporary reduction in automobile production

Industrial Production
(Index, 2000 = 100)



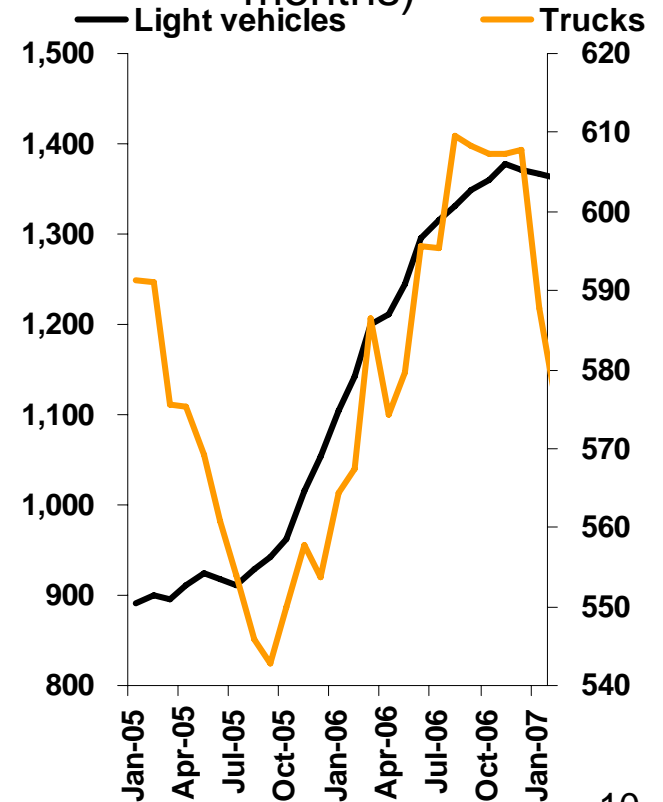
Source: INEGI and the Federal Reserve.

Exports
(real annual change, %, 3m mov. avg.)



Source: INEGI.

Automotive Production in Mexico
(thousand units, last 12 months)

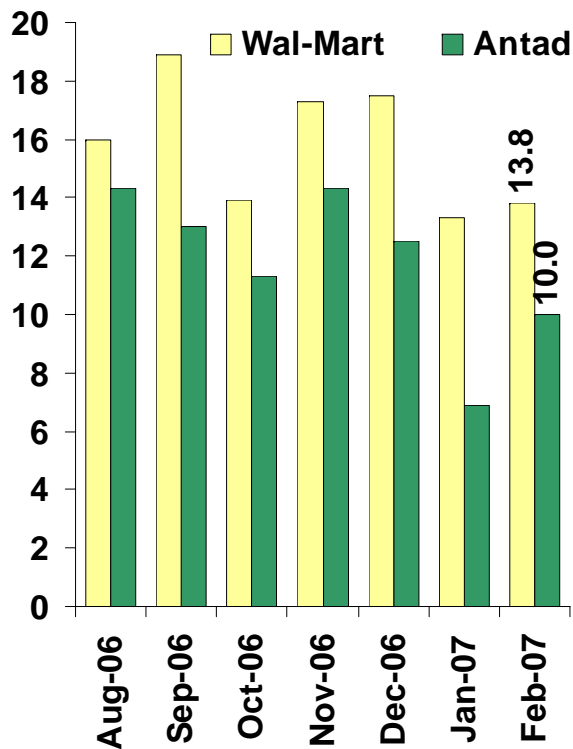


Source: AMIA.

Recent sales data, investment plans by department store chains, and the growth of credit suggest that consumption will maintain its dynamism. Sustained investment growth in 2007 is expected on the basis of the favorable evolution of producer confidence.

Sales: Antad and Wal-Mart

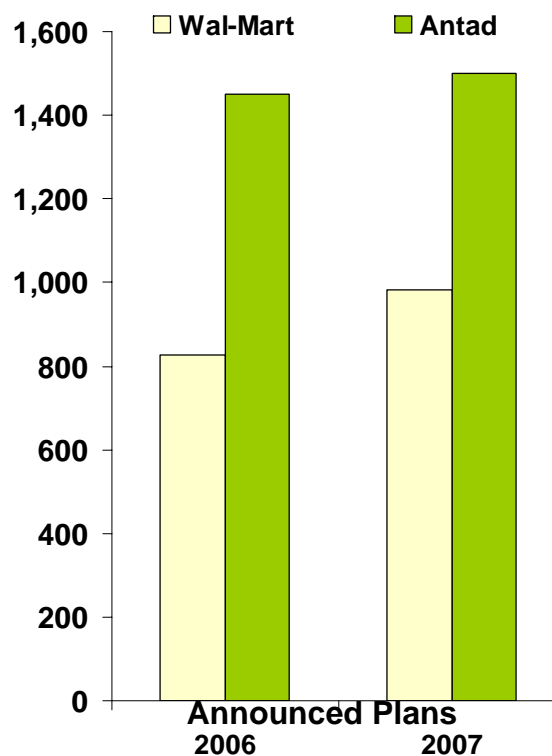
(real annual change, %)



Source: Antad and Wal-Mart.

Investment: Antad and Wal-Mart

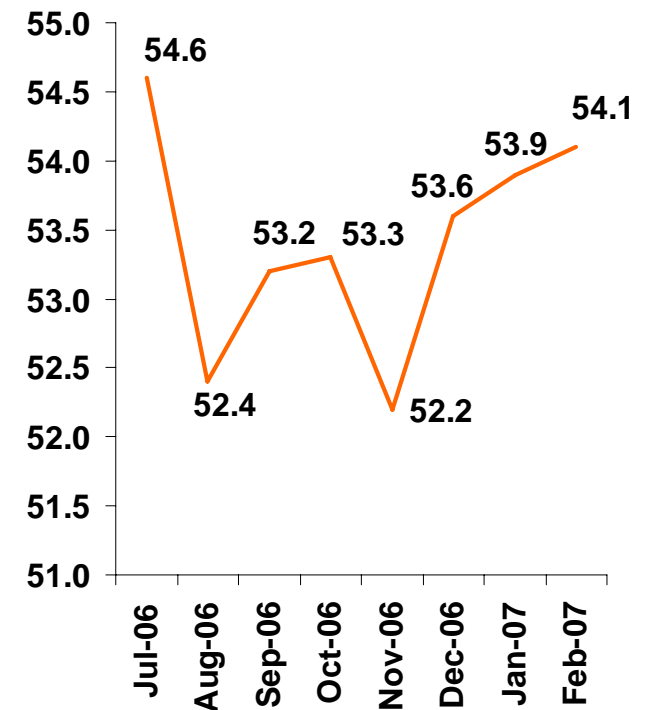
(million dollars)



Source: Antad and Wal-Mart.

Producer Confidence Index: Manufacturing Sector

(points)

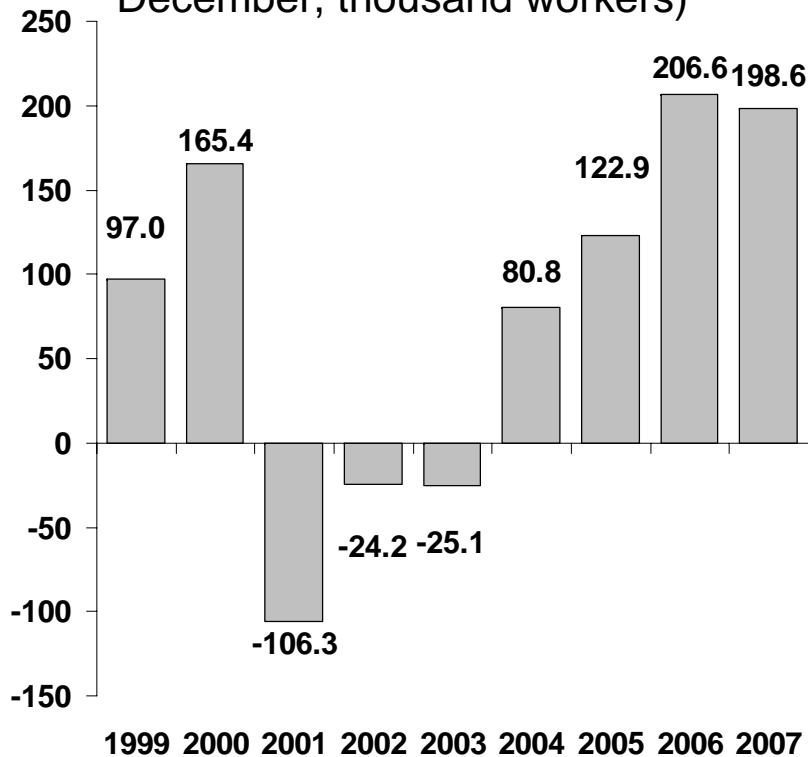


Source: INEGI.

Recent employment figures reflect this expected growth. This is the second consecutive year in which formal employment grows in January and February, and the increase in the first half of March is the largest since 1998.

Formal Employment Growth until the first half of March

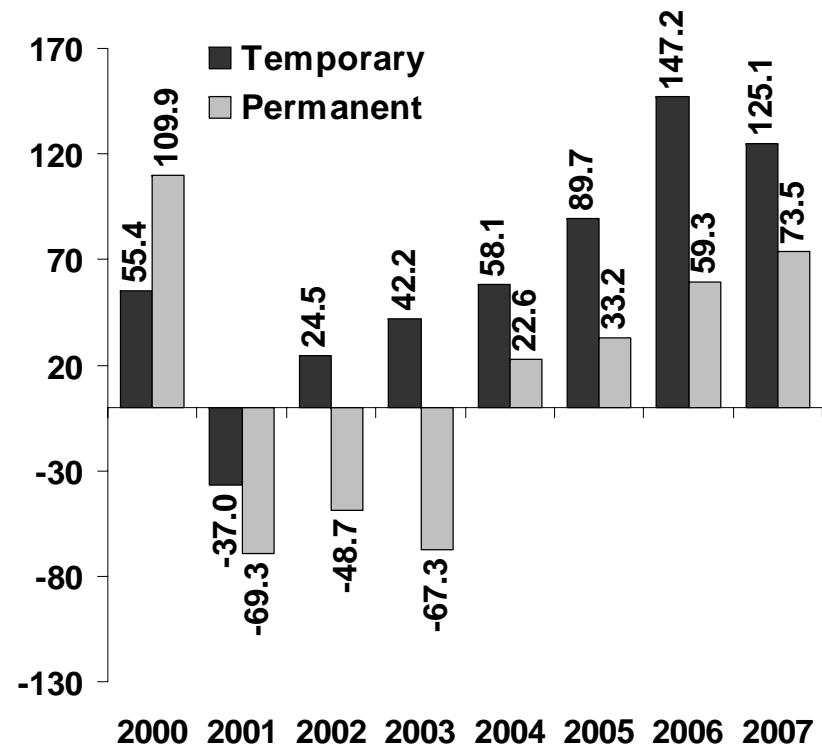
(accumulated change with respect to December, thousand workers)



Source: IMSS.

Formal Employment

(annual change, first half of March vs December, thousand workers)

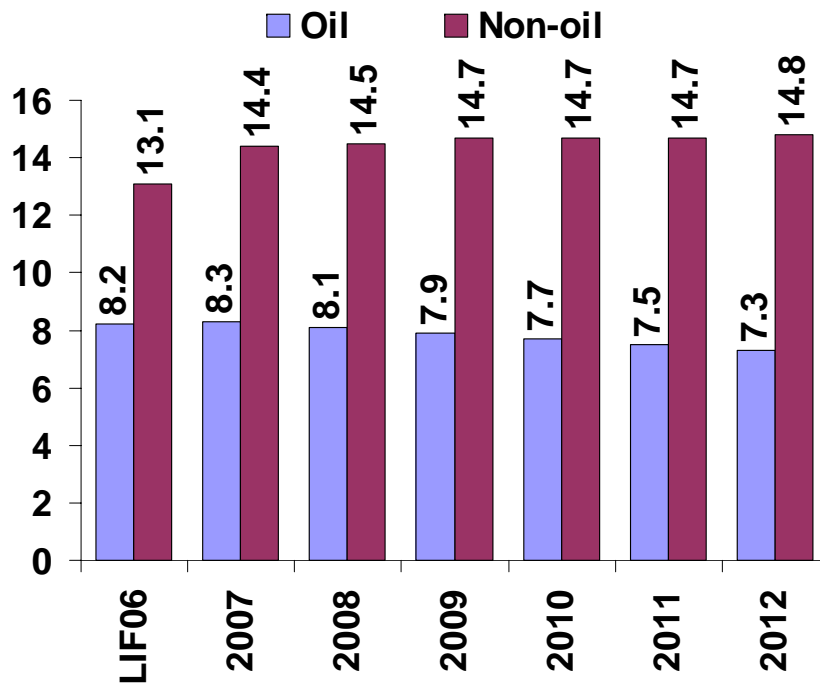


Source: IMSS.

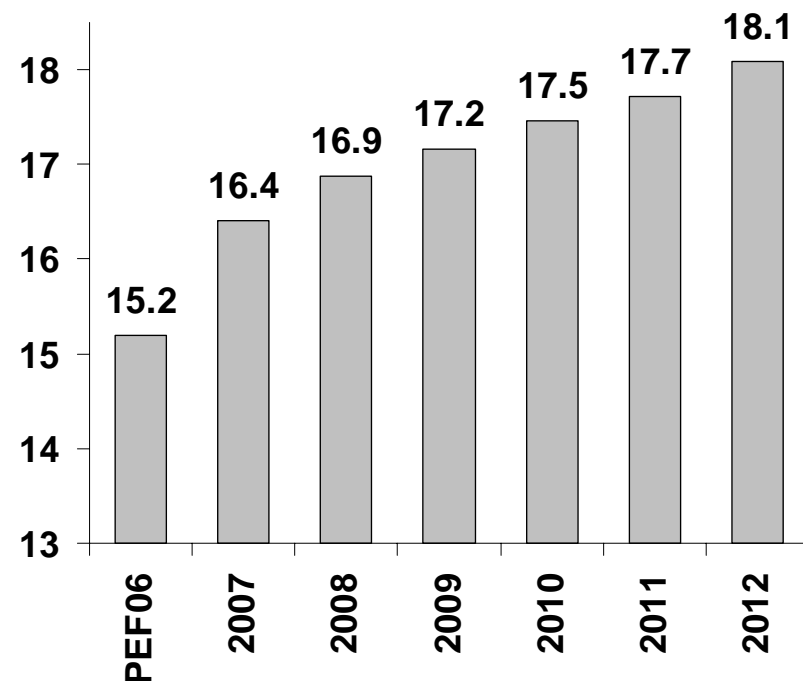
Public finances will continue facing important challenges during the rest of the Administration.

- A decrease in oil revenues as a percentage of GDP is expected during the next six years. This will be partially compensated by efficiency gains in tax collection.
- Expenditure pressures are due to expenditure on pensions and PIDIREGA projects.

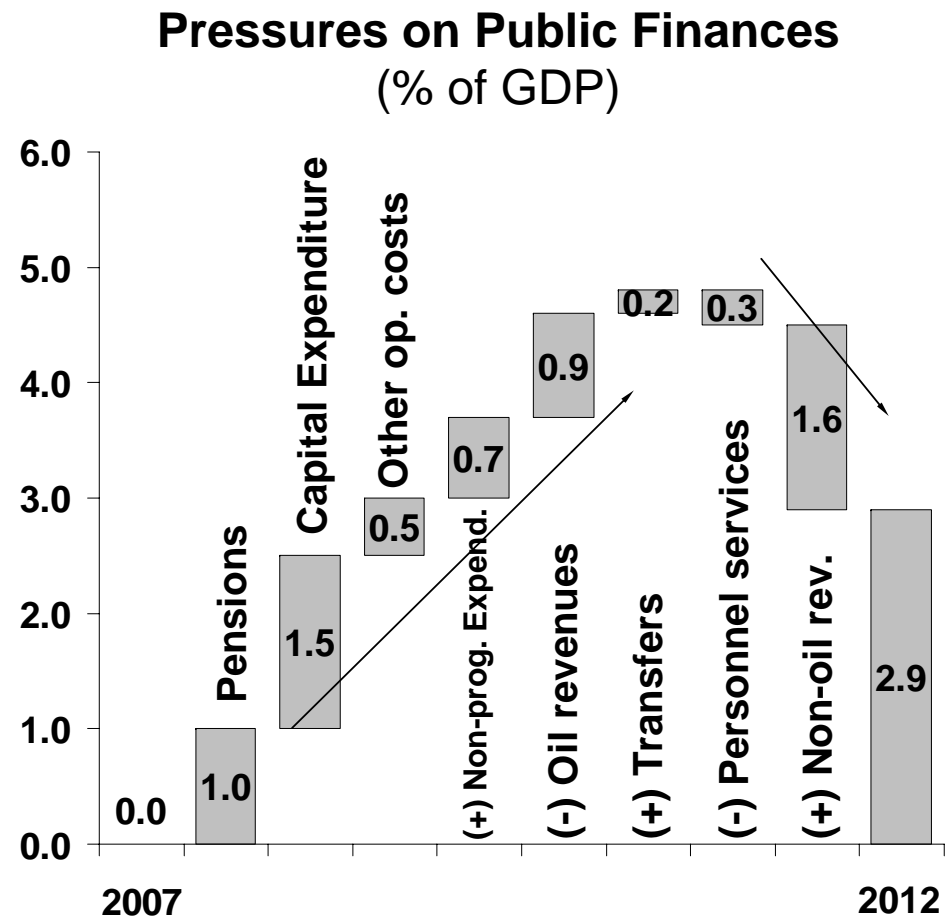
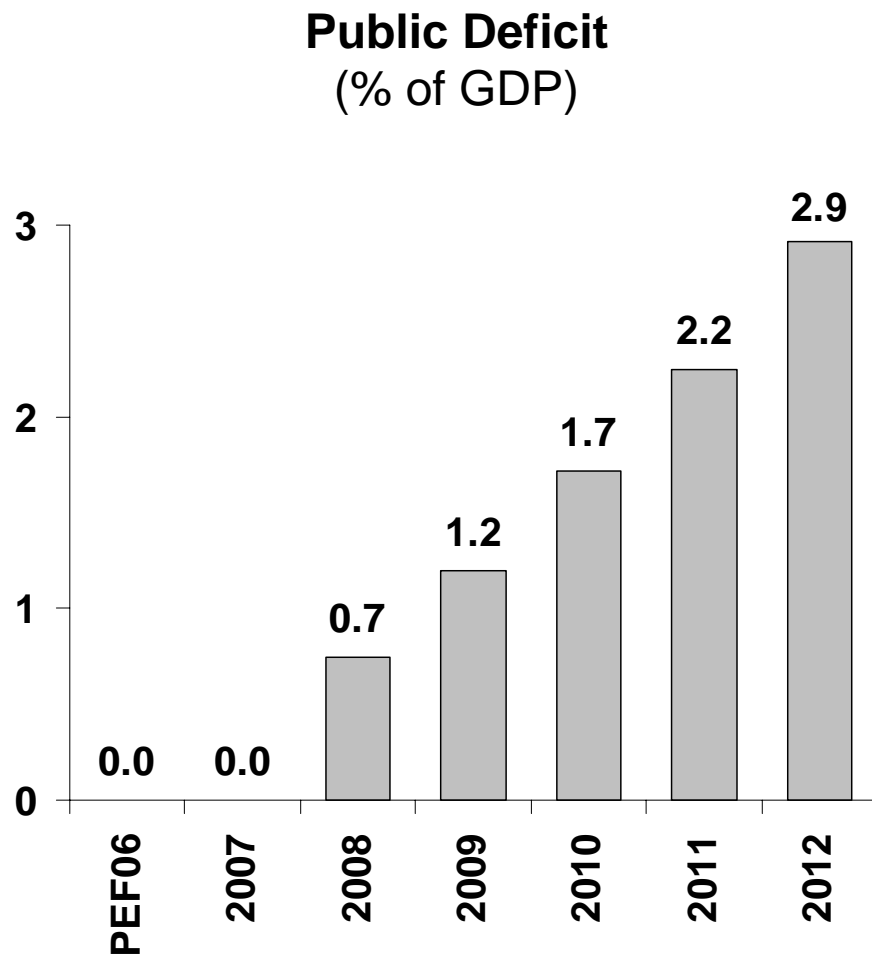
Budgetary Revenues
(% of GDP)



Programmable Expenditures
(% of GDP)



The higher expenditure growth would result in an important deterioration of the public balance.



In order to propose a fiscal reform, some pre-requirements are needed:

- **On the expenditures side:**
 - **Reinforcing transparency and accountability.**
 - **Guaranteeing a more efficient use of resources.**
 - **Allocating more resources to social and economic development spending.**
- **On the revenue side:**
 - **Attending the claim that not everybody pays taxes, promoting a fair tax burden and reducing fiscal evasion.**

Some of these pre-requirements are included in the Economic Program for 2007.

Going further, the fiscal reform that we would like to implement should include the following elements:

- **A diversification of the revenue structure that helps reduce the vulnerability of public finances to oil price volatility and to possible future reductions in the oil production platform.**
- **The relation between the Federal Government and Federal entities should be set on a more solid base.**

The current pension system for public sector workers is not financially viable and benefits are lost if workers move from the public to the private sector

1. Financial Insolvency

- The increase in life expectancy and the reduction in the age of retirement lead to insolvency
- **With the reform we would attain savings in net present value terms of more than 20% of GDP.**

2. Lack of mobility

- Workers that change jobs between sectors lose their benefits.

	1975	2005
Life expectancy at birth (years)	64.4	75.7
Average retirement age (years)	61.9	55.0
Average years receiving pension	2.5	20.7
Workers per pensioner	20	4

The reform distinguishes between three generations of workers:

- *Current pensioners* would not be affected by the reform.
- The benefits acquired until the date of the reform are recognized for *current workers*, who are offered two different alternatives of pension system going forward.
- The *new generation of workers* enters a system of individual pension accounts which makes them financially viable and fair.

Characteristics of the new pension system:

- **Defined contribution.**- Each worker has an individual account where both his/her and the government contributions' are deposited.
- **Individual savings.**- When workers retire they receive a pension on the basis of the resources in the account plus interest on these resources.
- **Voluntary savings.**- To strengthen workers' pensions, the government offers an incentive for each additional peso saved by the workers.
- **Mobility.**- By having individual accounts, workers keep their savings when they change jobs.
- **Workers' decision.**- After accumulating savings for a minimum pension, the workers can choose their retirement age depending on the size of pension they desire.
- **The government guarantees a minimum pension.**