Mexico’s Political, Policy, and Security Outlook: 2018 and Beyond
Mexico City ● October 9, 2017
2017 State and Local Elections Results: A Mixed Bag

**Highlights**

- On June 4, 2017, the State of Mexico held a gubernatorial election, Coahuila and Nayarit held both gubernatorial and local elections, and Veracruz held local elections.
- The PRI gubernatorial candidates won the State of Mexico and Coahuila, two states that have been governed by the PRI since the party’s founding.
- A PAN-PRD coalition candidate won Nayarit, the second time Nayarit will have a non-PRI governor.
- Morena proved extremely competitive in the State of Mexico, though unsuccessful.
- Coahuila’s electoral results are being contested by opposition parties in the Federal Electoral Court (TEPJF).

**Key Takeaways**

- Despite the fact that the PRI managed to retain two of its strongholds, the recent elections left the party in a weak position.
- In the State of Mexico, the PRI received a million fewer votes than in the 2011 governor election, and in Veracruz it no longer governs any of the state’s ten largest cities.
- Morena’s loss in the State of Mexico greatly hurt AMLO’s presidential prospects. The party had the opportunity to form an alliance with the PRD, which could have changed Morena’s fortunes in the race, but it declined.
- The electoral competitiveness of the PAN-PRD coalition was confirmed by the gubernatorial win in Nayarit and widespread municipal victories in Nayarit and Veracruz.

**2017 Gubernatorial Elections Results**

<table>
<thead>
<tr>
<th>State</th>
<th>Governing Party</th>
<th>Winner</th>
<th>Runner Up</th>
<th>Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mexico</td>
<td>PRI</td>
<td>PRI</td>
<td>Morena</td>
<td>2.8</td>
</tr>
<tr>
<td>Coahuila</td>
<td>PRI</td>
<td>PRI</td>
<td>PAN</td>
<td>1.5</td>
</tr>
<tr>
<td>Nayarit</td>
<td>PRI</td>
<td>PAN-PRD</td>
<td>PRI</td>
<td>11.9</td>
</tr>
</tbody>
</table>

Source: EMPRA, based on local electoral agencies

**Other Considerations**

- The election results revealed stronger voter support for opposition parties.
- With 13 percent of the national voter base, the State of Mexico has historically been considered an important testing ground for the presidential election.
- Voter turnout in the State of Mexico was 52.5 percent, while in the past presidential election (2012) it reached 63.4 percent.
Mexico’s Political Distribution Ahead of the 2018 Election

<table>
<thead>
<tr>
<th>Party</th>
<th>States</th>
<th>% of Electorate</th>
</tr>
</thead>
<tbody>
<tr>
<td>PRI, PRI-PVEM</td>
<td>15</td>
<td>46</td>
</tr>
<tr>
<td>PAN, PAN-PRD</td>
<td>12</td>
<td>33</td>
</tr>
<tr>
<td>PRD-PT</td>
<td>4</td>
<td>16</td>
</tr>
<tr>
<td>Independent</td>
<td>1</td>
<td>4</td>
</tr>
</tbody>
</table>

Source: EMPRA

Lower House

<table>
<thead>
<tr>
<th>Party</th>
<th>Seats</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>PRI</td>
<td>205</td>
<td>43</td>
</tr>
<tr>
<td>PAN</td>
<td>109</td>
<td>23</td>
</tr>
<tr>
<td>PRD</td>
<td>52</td>
<td>11</td>
</tr>
<tr>
<td>Morena</td>
<td>48</td>
<td>10</td>
</tr>
<tr>
<td>PVEM</td>
<td>40</td>
<td>8</td>
</tr>
<tr>
<td>Others</td>
<td>21</td>
<td>4</td>
</tr>
</tbody>
</table>

Senate

<table>
<thead>
<tr>
<th>Party</th>
<th>Seats</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>PRI</td>
<td>55</td>
<td>43</td>
</tr>
<tr>
<td>PAN</td>
<td>38</td>
<td>30</td>
</tr>
<tr>
<td>PT</td>
<td>15</td>
<td>12</td>
</tr>
<tr>
<td>PRD</td>
<td>8</td>
<td>6</td>
</tr>
<tr>
<td>PVEM</td>
<td>7</td>
<td>5</td>
</tr>
<tr>
<td>NA</td>
<td>5</td>
<td>4</td>
</tr>
</tbody>
</table>

Source: EMPRA
Political Dynamics Ahead of the 2018 Election

Intra-Party Dynamics

- The PAN and the PRD seem intent on pursuing a broad opposition coalition: Frente Ciudadano por México (FCPM)
- The FCPM has enormous electoral potential, as it provides an alternative to both the PRI and the intransigent politics of Lopez Obrador
- The project faces key challenges stemming from internal opposition in the PAN and PRD to the coalition and from personal political ambitions of members from both parties
- The PRI has changed its own rules to allow for a citizen candidate to obtain the party’s presidential nomination
- Morena’s primaries for Mexico City Mayor resulted in a split between AMLO and one of his main political operators
- In June, the National Indigenous Council (CNI) chose Maria de Jesus Patricio “Marichuy” to represent Mexico’s indigenous communities in the presidential election as an independent candidate

Mistrust of Electoral Institutions

- The recent state elections had a negative impact on public confidence in the National Electoral Institute’s (INE) capacity to oversee next year’s elections
- In a poll published by Reforma in June, 55 percent of those surveyed stated that they do not see the INE as an independent referee

Slight Recovery in Presidential Approval Rating

- President Peña Nieto’s ratings have recovered slightly after hitting rock bottom in January
- Mexicans are most concerned about public safety, though corruption and economic performance also poll among the most important issues to the general public

Citizens’ Main Concerns

- Public Safety: 53%
- Corruption: 16%
- The Economy: 11%
- Unemployment: 8%
- No Response: 12%

Source: EMPRA, based on Reforma

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2018 Presidential Elections: The Clock Is Ticking

**Up for Grabs**
- 2018 has the largest number of positions up for election ever in Mexican history: **3,406 public positions** up for election (629 at the federal level and 2,777 at the local level)
- As of the 2014 political reform, state and federal lawmakers, as well as mayors, to be elected in 2018 will be eligible for reelection for the first time in history

**Election Calendar**
- December 14 to February 11: primary elections
- March 29: deadline to register candidates
- March 30 to June 28: campaign period
- Sunday, July 1: election day

**Potential Voters**
- 86.8 million citizens
- 40% are millennials (ages 18-34)
- Citizens from Mexico City, Veracruz, Puebla and Oaxaca comprise 30% of the electorate

**What Is at Stake?**
- The consolidation of the reform agenda devised by the Peña Nieto administration
- The fight against corruption and impunity
- The strategy to combat organized crime and reduce violence
- Policies to reduce poverty and inequality
- Mexico's role in the international arena, including issues such as trade and investment and climate change
- Influence of civil society over the government agenda
- The fairness of the electoral system and the viability of independent candidates

*Source: EMPRA, based on INE*
2018 Presidential Elections: The Clock Is Ticking

Roster of Candidates

- Meade
- De la Madrid
- Narro
- Osorio Chong
- Nuño
- Anaya
- Zavala
- Moreno Valle
- Mancera
- Aureoles
- Barrales
- External Candidate
- Lopez Obrador

2018 Presidential Electoral Preferences (July 23)

- Morena: 28%
- PAN: 23%
- PRD: 17%
- Independent: 10%
- FCPM: 6%
- Verdes: 5%
- Other: 11%

Source: EMPRA, based on Reforma

Two-tier Scenarios (September 13)

- PAN
- PRD
- Morena
- PRD
- PAN

Mexico’s Political, Policy, and Security Outlook

- This is the third consecutive time that Lopez Obrador will run for president
- He is the candidate with the highest name recognition, but the highest rejection rate, at 38%
Voter Behavior and Other Considerations

Some Insights into Voters Behavior
Using the June 4 election State of Mexico as a proxy (El Financiero’s Exit Poll), a few conclusions can be drawn:

• 19% decided whom to vote for on Election Day

• Millennials seem less likely to vote for the PRI than older voters: 29% of millennials voted for the PRI vs. 37% of voters aged 34 and up

• Voters who only completed elementary school are more likely to vote for the PRI than college-educated voters: 43 percent of them voted for the PRI vs. 18 percent of college-educated voters

Politics After the Earthquake
The earthquake left more than 360 people dead, caused widespread destruction, and largely disrupted daily life and economic activities in Mexico City and some areas in the states of Morelos and Puebla

Political Ramifications

• Some analysts argue that the anti-government sentiments that emerged from the earthquake will likely end up hurting the ruling party (PRI) in 2018

• The bulk of voters in the Mexico City metropolitan area—where civil society proved strongest, and where animosity toward politicians is concentrated—would not vote for the PRI anyway

• Clear-cut assumptions are simplistic. The Federal Government focused its relief efforts on the states of Mexico, Puebla, Morelos, and previously in Oaxaca

• Andres Manuel Lopez Obrador was largely absent during the somber days that followed the earthquake

• The less disrupted party would be the PAN. The party didn’t show leadership in the wake of the earthquake, but the party-led coalition has embraced and promoted popular citizen initiatives

• It is unlikely that the rise of civil society in Mexico City will evolve into a political movement; rather, it is likely to manifest in particular initiatives to fight corruption at the local level

• The earthquake reopened the debate about the excessive cost of the Mexican electoral system and might result in a reduction of the public funds allocated to the country’s political system, one of civil society’s long-time demands
Rising Violence: Key Trends

• 2017 is on track to be the most violent year of the Peña Nieto administration, with an average of 70 homicides per day—25 percent higher than in 2016

• Just like the violence that characterized the 2010-2011 period, the violence is gruesome, often designed for public display, and shows no signs of abating

• Attacks on journalists, government officials, and local law enforcement are on the rise; the discovery of clandestine graves is also becoming more common

• Violence and criminal activity are expanding into tourism-oriented states such as Baja California Sur and Quintana Roo

Causes of Violence

• The high levels of violence observed over the past year and a half can be attributed in large part to the territorial expansion of the CJNG which has led to increased fighting among rival criminal organizations

• The re-arrest and extradition of Joaquin “El Chapo” Guzman caused turmoil, as rival criminal organizations have sought to expand into the Sinaloa Cartel’s domain

• Local gangs are becoming increasingly violent and often infiltrate local politics, which allows them to operate with impunity and affords them access to government and intelligence

Worsening Security Situation

Fuel Theft: Alarming Expansion

- Over the past seven years, illegal taps along the Pemex pipelines have increased by 1,388% from 642 in 2009 to 6,837 in 2016
- 5,789 clandestine fuel taps have been found from January to July 2017
- The Comptroller General’s Office (ASF) estimates that Pemex loses 4.1 million liters per day to theft, which is eight percent of its total production
- In 2016, fuel theft cost the country more than MX$30,836 million (US$1.7 billion)
- The bulk of fuel theft is carried out by small cells as opposed to large criminal organizations

Public Frustration with Government

- The government’s current anti-crime strategy has not been able to curb violence or criminal activity
- The new crime wave is affecting larger segments of the population and business sector than ever before, resulting in an incipient push by civil society to be included in the policy-making process
- Mexico ranked 66th out of 69 countries in the UDLAP’s 2017 Global Impunity Index

Economic Impact

- It is estimated that violence and criminal activity inhibits GDP growth by 2.7 to 3.3 percent, although views vary among economists and analysts

Illegal Taps Reported by Pemex 2009 - 2017

Public Security Perception Survey (ENVIPE-INEGI)

<table>
<thead>
<tr>
<th>Population that feels unsafe</th>
<th>Unreported crimes</th>
</tr>
</thead>
<tbody>
<tr>
<td>74%</td>
<td>94%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Homes with at least one crime victim</th>
<th>Adult victims of crime</th>
</tr>
</thead>
<tbody>
<tr>
<td>34%</td>
<td>22%</td>
</tr>
</tbody>
</table>

Source: EMPRA, based on Pemex
Source: EMPRA, based on INEGI, 2016 data

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National Anticorruption System: State of Affairs

State of Affairs

- According to the National Anticorruption System’s (SNA) bylaws, the system should have been operating at full capacity by mid-July, at both the federal level and in all 32 Mexican states.
- However, key pending appointments, a lack of funds, and problems with legislation at the local level seem poised to delay the system’s operation as well as its overall effectiveness.
- At the state level, the system is moving forward with several issues, including overwhelming evidence of conflicts of interest.

Details

- The appointment of the Special Anticorruption Prosecutor has been pending since late 2014 because of procedural objections from political parties and political gridlock.
- Since the appointment must be discussed and approved alongside a new law on the restructuring of the Attorney General’s Office (FGR), the process could take up to a year.
- Given how common and deeply entrenched corruption is in the public sphere, particularly at the local level, public officials from all parties have little incentive to build a strong SNA.
- Although the SNA can function in its current state, it has deficiencies that will not be easy to overcome.

Unaccounted Public Funds (Suspected Embezzlement), 2015

<table>
<thead>
<tr>
<th>State</th>
<th>Governing Party</th>
<th>Lost Funds (MX$ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Veracruz</td>
<td>PRI</td>
<td>10,007</td>
</tr>
<tr>
<td>Puebla</td>
<td>PAN</td>
<td>4,553</td>
</tr>
<tr>
<td>State of Mexico</td>
<td>PRI</td>
<td>4,010</td>
</tr>
<tr>
<td>Michoacan</td>
<td>PRI</td>
<td>3,222</td>
</tr>
<tr>
<td>Oaxaca</td>
<td>MC</td>
<td>3,137</td>
</tr>
<tr>
<td>Guerrero</td>
<td>PRD</td>
<td>2,717</td>
</tr>
<tr>
<td>Chiapas</td>
<td>PVEM</td>
<td>2,216</td>
</tr>
<tr>
<td>Jalisco</td>
<td>PRI</td>
<td>2,050</td>
</tr>
<tr>
<td>Nuevo Leon</td>
<td>PRI</td>
<td>997</td>
</tr>
<tr>
<td>Mexico City</td>
<td>PRD</td>
<td>920</td>
</tr>
<tr>
<td>Zacatecas</td>
<td>PRI</td>
<td>865</td>
</tr>
</tbody>
</table>

Source: EMPRA based on ASF

Mexico's Ranking in TI's 2016 Corruption Perceptions Index

Source: EMPRA based on Transparency International
Economic Outlook

Growth Despite Uncertainty

- Mexico’s GDP is expected to grow 2.3 to 2.5% in 2017
- Political uncertainty has not discouraged investment; the uncertainty about NAFTA eased when the markets noted that US priorities do not seem to be aimed at restricting access to markets
- Consumer spending has held steady despite inflation, as job growth has compensated for the loss of purchasing power
- The manufacturing sector has recovered, despite the drop in oil prices
- The amount of residential and private construction increased year-on-year in 2017; government investment in construction has been negatively affected by public spending cuts

The Earthquake's Economic Impact

- The extent of the economic damage is still unknown. Economists mostly agree that quake-related harm to economic growth will be short-lived, though the tourism sector may suffer until the first quarter of 2018
- Conversely, the quake may be a boon for the construction sector, potentially boosting GDP growth next year
NAFTA Negotiations and Country Priorities

Modernize conflict resolution mechanisms to make them faster and more transparent

Eliminate both Chapter 19 and the global safeguard exclusion

Expand international commerce, which may result in balanced trade

Improve trade balance and reduce the US trade deficit

Establish international systems that reduce corruption affecting trade and investment

Require member countries to punish government corruption and to keep proper records of corruption cases

Grant priority access to North American labor markets and educational opportunities for workers from NAFTA countries

Codify and enforce international labor laws in the renegotiated agreement

Leave rules as they are

Increase the percentage of NAFTA origin of goods

Priority Industries
- Financial Services
- Textiles and Apparel
- Agriculture
- Energy
- Telecommunications
- Digital Goods

Shared US-Mexico Modernization Demands
- Create enforceable environmental protections
- Protect intellectual property rights more effectively
- Aid small and medium-sized businesses
- Set regulations for energy trade
- Promote the exchange of information among NAFTA countries

Negotiation Timeline

<table>
<thead>
<tr>
<th>Round 1</th>
<th>Round 2</th>
<th>Round 3</th>
<th>Round 4</th>
<th>Several More Rounds</th>
<th>General Version of Agreement</th>
<th>Detailed Version of Agreement</th>
<th>Agreement Signed</th>
</tr>
</thead>
</table>
Key Developments in the Hydrocarbon Sector: Upstream

Mexico’s 5-Year Tendering Program for E&P

Past Tenders

• Seven completed rounds, 70 awarded contracts expected to result in a cumulative committed investment of US$2.4 billion
• The awarded contracts have resulted in the drilling of 104 wells: 66 for exploration and 38 for development
• In the case of commercial success, investments could total US$50 to $60 billion (when considering Trion)
• Contracts awarded to more than 66 companies from 17 countries including BP, Total, Shell, Eni, Repsol, Citla, Premier, and Lukoil

Recent Discoveries
• In March 2017, Italian oil company Eni became the first international company to discover reserves (light crude oil) since the reform was enacted
• In July 2017, the consortium of Sierra Oil & Gas, Talos Energy, and Premier Oil discovered an estimated 1.4 - 2.0 billion barrels of light crude oil, making it among the largest shallow water fields discovered globally in the past two decades

Upcoming Tenders and Farmouts
• Pemex Farmouts: 1) Ayin-Batsil, Ogarrio, Cardenas Mora: Oct 4, 2017; 2) Nobilis-Maximino: Jan 2018; 3) Ayin-Batsil, Ayatsil-Tekel-Utsil and Chinchontepec, as well as shallow water areas, on-shore, and shale-gas: before the end of 2018
• CNH Tenders: Round 2.4 of deepwater and shale fields: Jan 31, 2018; Round 3.1 of shallow water fields: March 27, 2018; Round 3.2 of deepwater and shale fields: end of 2018

Crude Oil & Gas Production

• Crude Oil: Pemex is expected to close the year with an average crude oil production of 1.94 million barrels per day, an 8 percent drop from its 2016 average.
• Natural Gas: Since 2016, the volume of natural gas imported by Mexico is higher than the amount of domestic production. The gap went from 709 MMcfd in 2016 to 1,863 MMcfd in June 2017, a 162% increase

Mexico’s Natural Gas Production vs. Imports (MMcfd)

Source: EMPRA, based on CNH
Key Developments in the Hydrocarbon Sector: Midstream and Downstream

Oil & Gas Infrastructure

• Before the end of 2018, Mexico will have 18,700 km of operational gas pipelines, 39% added during President Peña Nieto’s term through investments of US$12.2 billion

• Currently, there are committed investments of US$15 billion in 22 projects for the development and expansion of storage, transportation and distribution of refined oil: 11 pipelines, four storage and distribution terminals, and seven railways

Refined Fuel Production

• Following a fire in Oaxaca’s Salina Cruz refinery (June), Pemex’s production of refined fuels reached a 27-year low in July 2017, with only 605,000 bpd produced on average

• In July 2017, Pemex refineries were working at 42 percent of their capacity; production of refined oil products declined 18.2 percent in a year; the recent high-magnitude earthquakes are expected to further hurt production

Refined Fuel Logistics and Retail

• Mexico’s demand for imported gasoline from the US, among other imported energy products, has been growing. The value of US energy exports to Mexico is now more than twice that of US energy imports from Mexico

• The liberalization of refined fuels logistics has triggered an estimated investment of US$2.3 billion in the construction of new pipelines. Today, Mexico imports close to 60 percent of its fuels, and 81 percent of its natural gas

• There are 21 companies that currently have fuel retail stations in Mexico, including BP, Chevron, Shell, Tesoro, and Costco Gas

Gasoline Production vs Imports

Source: EMPRA, based on Pemex
Electricity and Renewables

Power Sector Reform

- Although Mexico’s hydrocarbons sector has garnered most of the attention, the regulatory changes to the Mexican power sector are similar in terms of their scope and potential economic impact.
- The reform includes significant changes throughout the electricity supply chain: power generation is set to become a fully competitive activity; an independent system operator will run a wholesale electricity market; and open access to the power grid will be guaranteed to all market participants.

Clean Energy Goals

- By 2031, Mexico plans to have 113,26 MW of capacity, a 55 percent increase from 2016, with half of the energy coming from clean sources.
- CFE plans to retire 137 power plants—mostly conventional thermoelectric plants—in favor of combined cycle, solar, wind, and nuclear power.
- Mexico plans to award clean energy certificates (CECs) to producers based on output and require large power consumers and suppliers to purchase CECs at a market-determined price, effectively using market dynamics to incentivize clean energy investment.

Overview of the Two Long-Term Power Auctions

- The launch of the wholesale electricity market in January 2016 brought Mexico’s electricity industry closer to modern standards of power generation and trading.
- 1st long-term auction (March 2016): 11 winning companies, which collectively submitted 18 proposals, largely solar and wind projects for the production of 2,085 MW of clean energy per year at between US$45 and US$55/MW on average.
- 2nd auction: 23 winning companies that will produce 3,916 MW of clean energy per year at US$33.47/MW on average, through a US$4 billion investment in new renewable projects.
- Currently, there are 35 private electricity companies with contracts and committed investments in the Mexican power sector.

November Auction

- The third electricity auction, planned for November, is forecasted to triple production of clean energy from 17,000 MW via investments of US$4 billion. The first two auctions generated US$6.6 billion in total investments.
## 2018: Main Electoral Platforms and Challenges Ahead

<table>
<thead>
<tr>
<th>Political Platform</th>
<th>Challenges Ahead</th>
<th>Likely Problems if Elected</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Continued consolidation of structural reforms</td>
<td>• Alienated citizenship</td>
<td>• Continued corruption and impunity</td>
</tr>
<tr>
<td>• A reformed PRI, cohesive party</td>
<td>• Convincing citizens that the party can change will be a daunting task</td>
<td>• The PRI will have to incorporate the PAN-PRD agenda</td>
</tr>
<tr>
<td>• Experience in government, capable technocracy</td>
<td>• Need to distance itself from PRI’s members accused of corruption (there are many)</td>
<td>• Social animosity against the party and the president</td>
</tr>
<tr>
<td>• At the center of the political spectrum</td>
<td></td>
<td>• Curbing Morena’s electoral expansion</td>
</tr>
<tr>
<td>• A broad political alliance that promises to embrace a citizen-led agenda</td>
<td>• Agreeing on an electoral platform that does not violate the principles of each party</td>
<td>• Lack of efficient political operators</td>
</tr>
<tr>
<td>• Priorities are anti-corruption reform, improved economic competition, and transparency</td>
<td>• Attracting voters from both sides of the political spectrum</td>
<td>• A divided congress and constant blackmailing from the PRI</td>
</tr>
<tr>
<td>• Best option for undecided voters that want the PRI out but are not convinced by AMLO’s rhetoric</td>
<td>• Agreeing on a method for choosing a candidate and agreeing on the actual candidate</td>
<td>• Morena’s electoral expansion and increasing influence in Congress</td>
</tr>
<tr>
<td>• Close to civil society and business sector</td>
<td>• Convincing the electorate, particularly undecided voters, that the coalition could be effective in carrying out its government plan</td>
<td>• Implementation of controversial reforms such as education, and anti-corruption</td>
</tr>
<tr>
<td>• Focus on the redistribution of wealth</td>
<td></td>
<td>• Potential conflicts within and between the parties that comprise the coalition</td>
</tr>
<tr>
<td>• Promise to reverse structural reforms, the NAICM project</td>
<td>• Convincing detractors that he doesn’t represent a threat to the country’s macroeconomic stability</td>
<td>• Mix of 1970s inward-looking economics combined with strong state intervention and a hefty dose of populism</td>
</tr>
<tr>
<td>• End alignment with the US in the international arena</td>
<td>• Finding allies who can help him garner votes without compromising his position</td>
<td>• Lack of technical credentials and a team capable of leading the federal government</td>
</tr>
<tr>
<td>• Change crime-fighting strategy</td>
<td>• Maintaining certain political correctness, having alienated potential allies in the political, civil society and business arenas</td>
<td>• A divided congress</td>
</tr>
<tr>
<td>• Promise to eradicate corruption</td>
<td></td>
<td>• Strong chance of his government sabotaging the energy and education reforms</td>
</tr>
</tbody>
</table>

High Public Debt
Political Instability
Violence and Lawlessness
Corruption and Impunity
Social Discontent

Improving Education
Protecting the Environment
Strengthening the Rule of Law
Macroeconomic Stability
Diversifying Trade and Investment

New Government 2018

Key Pending Reforms

<table>
<thead>
<tr>
<th>Economic</th>
<th>Rule of Law</th>
<th>Political</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Tax Reform</td>
<td>• Unified Police Command</td>
<td>• Second round for presidential and gubernatorial elections</td>
</tr>
<tr>
<td>• Pension Reform</td>
<td>• Internal Security Law</td>
<td>• Public funding for political parties</td>
</tr>
<tr>
<td>• Minimum wage</td>
<td>• Deepening anti-corruption legislation</td>
<td>• Reducing Congressional seats</td>
</tr>
<tr>
<td>• Energy Trade within NAFTA</td>
<td>• Money laundering</td>
<td></td>
</tr>
<tr>
<td>• Pemex’s fiscal regime</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Key Risks Ahead

Political Arena
• New corruption scandals could deliver a final blow to the Peña Nieto administration and the PRI, and further empower Lopez Obrador
• Infighting within the PAN could still undermine the success of a PAN-PRD coalition
• Primary election processes have started to generate conflicts between parties, while also impeding cooperation on key legislation
• The road to the 2018 elections is unlikely to be a smooth one…

Rule of Law and Public Security
• Violence could reach even higher levels as the election approaches
• Persistent insecurity in the states of Mexico, Michoacan, Tamaulipas, and Guerrero, among others, has resulted in capable law-enforcement entities being stretched too thin. With an insufficient number of well-trained officers deployed in these crisis states, security strategies are at risk

NAFTA and Other Macro Risks
• President Donald Trump could renew his attacks on Mexico and NAFTA in order to galvanize his base
• Industry analysts foresee a drop in oil prices in 2018, which would negatively affect Mexico’s GDP growth prospects
• Political uncertainty (e.g. Lopez Obrador gaining ground in the polls) may discourage foreign investment

Energy Sector
• The potential departure of Gonzalez Anaya from Pemex could interrupt key internal reforms and add uncertainty to the upcoming farmouts
• Land dispute issues continue to delay onshore hydrocarbon, electricity and infrastructure projects, particularly in southern Mexico, a trend that could intensify if Lopez Obrador were to win the presidency
Conclusions

Electoral Outlook
- The most probable scenario is an election between three main contenders: PRI, FCPM and Morena. With less than a year until the presidential election, there is no clarity as to which party or candidate is likely to win.
- Each party’s prospects will be easier to assess around December when electoral strategies are defined and candidates are selected.

Incumbent Administration
- Despite the massive corruption scandals affecting the party, the PRI may have a chance at remaining in power if the party chooses the right candidate.
- Improved economic growth, a successful renegotiation of NAFTA, and an improved security outlook could increase support for the PRI; the PRI’s emergency response to the earthquakes and its leadership during rebuilding and recovery will also influence the party’s presidential prospects.

Political Opposition
- The chances of Lopez Obrador running a successful presidential campaign are slim but could improve if there is infighting within the PRI or the PAN-PRD coalition, or if new PRI corruption scandals emerge.
- The likelihood is high that the PAN and the PRD will consolidate its coalition for the 2018 presidential election. Its potential success depends on whether the parties develop a coherent platform and nominate a strong candidate.
- It is likely that whoever wins will not have a majority in Congress, which will force the new government to depend on support from other parties in order to implement its government program.

Rule of Law
- Insecurity, lawlessness, corruption, and a weak justice system—along with high rates of poverty and a huge lag in education—remain the country’s most acute obstacles to sustained economic growth, social development, and political stability.
- Security issues will remain a long-term problem for the foreseeable future. Ignoring the issue will only preclude a much needed debate, ultimately delaying the crafting of viable solutions.
- The next administration needs to promote a comprehensive, long-term strategy that tackles corruption and increases accountability at the local level.
About EMPRA

Emerging Markets Political Risk Analysis (EMPRA) is Mexico’s leading political risk advisory firm. EMPRA delivers critical intelligence and independent analysis of political, policy, and security developments and their impact on key areas of the economy. Our services help decision makers anticipate upcoming changes in the political spectrum and formulate timely, successful strategies in the face of sudden changes and uncertainty. This has a direct impact on investment, decision making, and corporate performance.

“The price of stability is continual awareness and active response to change”