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Statement by Mr. Andrianarivelo, Mr. Nguema-Affane, and Ms. Nankunda on Mexico (Preliminary)
Executive Board Meeting
November 2, 2020

We thank staff for their well written set of papers and Mr. Mr. Guerra and Ms. Arevalo Arroyo for their insightful Buff statement.

Mexico has been hardly hit by the COVID-19 pandemic as evidenced by the severe but improving epidemiological situation, significant job and income losses, and a large economic contraction. We commend the Mexican authorities for their appropriate yet measured response to the pandemic compared to peers. We understand that under the current policy stance and given the high uncertainty around the pandemic it could take years for employment and incomes to return to pre-crisis levels, thereby compounding the long-standing challenge of achieving strong and inclusive growth. We therefore agree that going forward, the authorities should use their policy space and strong policy frameworks to ramp up their pandemic-mitigation efforts and support the ongoing economic recovery. Sustaining momentum of reforms aimed at strengthening governance, tackling corruption and addressing informality will be essential to improve business environment and take advantage of the USMCA that came into force in July 2020. The authorities' priority put on strengthening the health response to foster a safe and robust reopening of the economy is in our view appropriate. We agree with the thrust of the staff appraisal and policy recommendations and would like to make a few comments for emphasis.

On fiscal policy: A greater near-term fiscal support will be critical to mitigate the impact of the pandemic and put the ongoing economic recovery on a sustainable path. While the authorities' efforts to contain debt vulnerabilities are welcome, we agree that the available fiscal space should be used towards higher health, social and infrastructure investment expenditures to contain the effects of the economy, notably the most vulnerable segments of the population. *We would appreciate staff indication on the extent of possible increase in public spending without triggering the FRL escape clause?*

On tax reforms, we share the authorities' view in Mr. Guerra's and Ms. Arevalo Arroyo's Buff statement that a tax hike is not politically and socially feasible in the middle of the pandemic and should be considered in better times. Social protection programs should be strengthened to improve targeting and help reduce high informality. *Could staff elaborate on the possible impediments to expand the unemployment benefits system existing in Mexico City to the whole nation?*

On monetary policy: The central bank ought to be commended for its prompt response to support the economy in this difficult time despite a limited use of related facilities by banks. The gradual monetary policy easing has been appropriate, and we encourage the Banco de México to remain prudent, vigilant and guided by data developments. Further monetary easing should be considered when inflation is firmly on a downward path, expectations remain well anchored, and uncertainty recedes. We note the concern that further policy rate cuts could trigger another wave of capital flows and increased stress in domestic markets. *Could staff indicate how domestic market stress have evolved in Mexico using the local stress index (LSI) developed recently by the IMF?* We commend the central bank for improving its communication strategy. We see merit in the authorities' stance regarding the consideration of a review of the monetary policy framework. *We would appreciate staff's reaction to the authorities' point*.

On financial sector policies: The financial sector remains resilient but continued close monitoring of small banks with large exposures is needed. We support the authorities' efforts to increase financial deepening and inclusion by leveraging technology. We encourage the authorities to strengthen the regulatory framework for supervision, the rapidly evolving Fintech industry and resolution and crisis management, notably by advancing the implementation of Basel III. We note that banks intend to resume the capital distribution despite the regulator's recommendation. *Could staff indicate to which extent banks' move reflect an improvement in their assessment of financial vulnerabilities?*

On structural reforms: We commend the authorities for the progress made in strengthening governance, transparency, AML/CFT and anti-corruption. The recent adoption of the National Anti-Corruption Policy and the update of the ML/TF National Risk Assessment is particularly noteworthy. We welcome their commitment to sustain structural reforms in these areas. We note that a draft law addressing gaps in the AML/CFT framework is pending in the Senate. *Staff assessment of this draft law is welcome*.