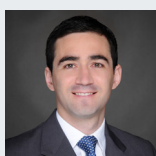


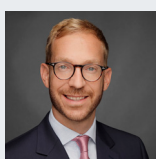


## Emerging Markets

# Analyst insights from Mexico



**Martin Baylac**  
Latin America Analyst



**Dan Hurley**  
Portfolio Specialist

Our investment and research teams travel regularly across emerging markets (EM) as a key part of their work to identify compelling investment opportunities for our clients, deepening long-term relationships with company managements and building new ones. These trips also give them the chance to meet with competitors, suppliers and customers to build a well-informed picture of what's really happening on the ground.

Members of our emerging markets team recently visited Mexico, Latin America's second-largest economy and one of the best performers in the EM universe in the first half of 2023. As at the end of June, the country constituted 2.6% of the MSCI Emerging Markets Index.

Dan Hurley, our Emerging Markets Portfolio Specialist in London, spoke with Latin America analyst Martin Baylac while he was in Mexico City to learn what he had discovered on his latest visit.

Starting in Guadalajara, Mexico's third largest city, before moving on to the capital, the team's meetings covered a number of different sectors including, mining, technology and financials, with a tilt toward infrastructure and consumer, both important constituents of the local economy.

### **Near-shoring impacts real but not yet universal**

According to Baylac, the mood was mostly "cautiously optimistic" among the companies and local people he had spoken to. Mexico 's economy has registered six consecutive quarters of growth (up to and including Q1 2023), buoyed by a strong labour market, consumption growth and an increase in tourism. Real rates, meanwhile, remain high at around 5.5% which has led to an appreciation in the currency, with the peso reaching five-year highs against the US dollar earlier this year. While he is cognisant of the view that the currency has appreciated too sharply over a short period, Baylac believes the peso is "relatively well anchored" and does not foresee a significant depreciation in the near term.

'Near-shoring' has become something of a buzz word when talking about Mexico's economy, a term used to describe the recent trend that has seen many US companies move production and supply chains closer to home, namely from China to Mexico. While Baylac admits the near-shoring story is "fundamentally very real" in Mexico, he says it is not a nationwide

phenomenon, being most visible in the northern states of the country closest to the US border. In addition, questions remain over how well the country can overcome the structural challenges that exist. He believes that “a lack of skilled labour, as well as significant logistical and infrastructure bottlenecks,” all need to be addressed for the country to really benefit from this trend longer term.

It will be a long and uneasy process but there has been “encouraging progress in some areas,” he believes. For example, labour force participation has been increasing, in particular among women, where historically participation has been low relative to other EM economies.

### 2024 elections keep politics on the agenda

On the political front, Mexicans are due to go the polls in mid-2024 to select their next President. Baylac will be keeping a close eye on developments and admits he is braced for more political uncertainty relative to the last few years. Current President Andrés Manuel López Obrador (also known by his initials AMLO) has brought in some more

populist measures in recent years, such as a rise to the minimum wage and more days off for workers which, along with the strong currency, Baylac says “are impacting company margins.” But there are also a number of more radical reforms in the pipeline which may test the country’s “independent and rational” Supreme Court after the summer recess, which could pose further risks.

Following the strong start to 2023, equity valuations exhibit more “mid-cycle plus levels” according to Baylac, but he says that “on aggregate, they are not expensive yet.” Given the stronger currency, he says he is looking closely at companies whose earnings are derived primarily from US dollars, so exporters and those that have meaningful operations outside of Mexico. It is exactly trips like this that he says help him and the team to gather invaluable insights, to identify pockets of strength within the country and the companies that are well-placed to benefit.

Next up for Baylac is a trip to China in September, with plans for the Middle East and Brazil later in the year.

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