Privest Vision 2025

Comercial Version

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I. Business Environment

2025 will not be a conventional year for Mexico:

- Regulatory and administrative changes could **create bottlenecks in regulations and government authorizations**.
- Only 8% of analysts consider it a good time to invest[1].
- **Debt** levels of **Pemex and CFE** with private suppliers and their effects on the banking system.
- Tariff dispute with the USA will affect exporting and importing companies, though there are opportunities in both sectors.
- Review of the USMCA (T-MEC).
- Changes in labor legislation and potential additional tax burdens.
- Increased insecurity due to migration.
- High real interest rates.
- Low probability of meeting the economic framework proposed by the government.
- Variable fiscal deficit, gaining attention from credit rating agencies.

Risks:

- **Escalation of geopolitical conflicts,** compounded by Trump (tariff and/or political reprisals).
- High **fiscal deficit in the USA**: pressure on inflation, interest rates, and growth.
- **Anti-immigration and tariff policies** in the USA, targeting Mexico (USMCA).
- **Inadequate management by the Mexican government**, with an economic plan offering little room for maneuver.
- **Global macroeconomic level:** possible tariff wars, decline in global trade, and higher levels of public deficit—slowing the reduction of inflation and resulting in higher interest rates and global deceleration.

II. 2025 Outlook

Following the **government changes** in 2024, the year presents an unprecedented scenario:

- **USA:** Trump with **broad leeway to implement** his economic policy, national security, and foreign policy strategies.
- **Europe: Gradual recovery** and price stability. The war in Ukraine threatens the balance of power.
- **Japan: Modest growth**, likely increase in interest rates, and JPY revaluation as a foundation for the stock market's performance.
- **China:** Structural weaknesses and higher US tariffs reducing growth and increasing deflation risks. To offset this, government stimulus programs include CNY devaluation, higher tariffs, or political measures.
- **Emerging Asia:** A potentially **winning region (Taiwan and India)** due to investment in AI and "friendshoring."
- **Mexico:** Effects of **Trump's measures** will remain a permanent source of **tension and volatility**. Mass deportations will affect employment, urban balance, and security. **Risks in inflation and growth**.
- **Attractive stock markets**, earnings growth mainly in the U.S. Investment in **AI**. **Selective** investment strategy.
- **Moderate reduction** in **inflation** and **interest rates**, corporate bonds as a profitability element, along with alternative products (preferred stocks, real estate investments, and private equity). Strong USD.

1. Survey on Private Sector Economists' Expectations December 16, 2024 – Banco de México

III. Economic Environment

2025 estimates (%)				
Indicators	**GDP**	**Inflation**	**Reference Rate**	**Public Balance***
Developed Markets	**1.7**	**3.0**	**3.1**	**-4.3**
USA	2.1	2.5	3.9	-6.5
Eurozone	1.0	2.0	2.2	-3.0
Japan	1.2	2.1	0.8	-3.8
Emerging Markets	**4.2**	**3.5**	-	**-4.6**
China	4.5	1.0	2.7	-5.5
India	6.5	4.2	5.8	-4.9
México	1.2	3.8	8.4	-3.9

Sources: *World Economic Outlook*, *Bloomberg*, Banco de México, *Federal Reserve Board*, CGPE 2025.

*: GDP%

- **Global GDP similar to 2024: 3.2%;** emerging countries will show the greatest dynamism. The deglobalization process will continue.
- **Industrialized countries: 1.7%** and **uneven**. The **USA** (2.1%) will remain the **strongest economy**. **India** will continue to be the **country with the highest growth** (6.8%). China will lose momentum, but this will be offset by other emerging Asian economies due to increased demand for semiconductors and AI-related electronic products.
- **Inflation will continue to decline** thanks to the efficient management of Central Banks, but the decrease will be **marginal**.

EUA

- **Trump's campaign offer**[2] **concentrated on domestic issues: migration, drug trafficking, and the economy** (reducing excessive federal spending and inflation, deregulation, cutting taxes for workers and businesses, USD as a global reserve currency, and the USA as a manufacturing powerhouse).
- **GDP: Stable growth (2.1%)** supported by **consumption** (65% of GDP) and investment (18% of GDP).
- Favored **sectors**: **AI**, the **financial sector**, **public services**, and **electricity generation**.
- **Inflation constrained** by potential increases in tariffs, services, and wage pressures (mass deportations). Likely shorter and shallower **monetary expansion cycle**.
- **Interest rates:** The Fed estimates that by the end of 2025, the federal funds rate will be at 4%, implying **two 25 basis point (bps) reductions in 2025**.
- **Strong USD** and continued preference as a reserve currency. **Uncertainty about** the **magnitude of the fiscal deficit** could be an additional limit for rate cuts.

Eurozone

- **GDP:** Close to **1.0% and uneven**. **Spain** will show **the best performance** due to its ties to the services sector. Manufacturing has been contracting for more than two years; Germany and France will grow more slowly. **Consumption will be an important component** (higher employment levels, real wages, and lower interest rates).
- **Inflation**: Will reach the ECB's target and continue the trend of lowering **interest rates**. Weak EUR in the first half of the year.
- **Sectors: Financial, defense, and aeronautics**, as well as **luxury consumption** (depending on China).

2. https://www.donaldjtrump.com/platform

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Japan

- **BoJ: A "virtuous cycle"** between rising wages, higher demand, inflation between 2% and 3%, improved corporate performance, and higher economic growth. **GDP: Around 1.0%,** supported by high employment levels and wage increases.
- The JPY reached its lowest levels since the 1990s. A recovery is expected as the BoJ continues to normalize monetary policy.
- Attractive **sectors: Financial, small- and mid-cap stocks, aeronautics, and technology.**

México

- New Government: Constitutional changes (judicial reform and dissolution of autonomous bodies, among others) and the new U.S. administration make 2025 **a year with multiple challenges**.
- **GDP: CGPE 2025** estimates growth **between 2-3%,** supported by consumption and investment, which have slowed since Q3 2023. Banxico's survey places it at **1.2%.**
- **Inflation: Gradual reduction** to 4.4%. **Analysts expect it to be 3.8% this year, higher than the Banco de México forecast** (3.3%). Key factors will include the behavior of service, food, and imported goods prices.
- **Interest Rates**: A 125 basis-point reduction in 2024 is expected. The **downward trend is anticipated to continue** this year. Banxico will conclude its cycle before the FED.
- **Increased Concerns** About Macroeconomic Stability: **Public deficit levels**. **Credit rating agencies have downgraded the sovereign debt outlook** from stable to negative (limited revenues, rigid spending structure, and PEMEX's financial situation).
- **Trump Element**: All priorities of his agenda have potential impacts on Mexico, including migration control, tackling drug trafficking, and protecting U.S. industries.
- Tariff Threats: Mass deportations and a potential remittance tax could put pressure on financial markets, not only affecting the exchange rate but also interest rates. These measures anticipate a lower flow of foreign currency. We expect an **average range between 20.00 and 21.50 pesos** per dollar, with higher volatility in the first half of the year.
- Government Popularity: The new administration begins with high popularity but is compelled to deliver immediate results in security and implement measures that facilitate private investment and job creation.

China

- **Double Challenge:** Address **structural weaknesses** and **counter external pressures** from U.S.-imposed tariffs.
- **GDP: 4.5%.** Transitioning the economic model towards reduced dependence on exports and greater emphasis on domestic consumption.
- To **Mitigate Trade War**: Expansionary monetary and fiscal policies, decreased demand for U.S. government securities, yuan (CNY) devaluation, and strengthening trade ties with other regions.
- **Negative Market Environment: Opportunities lie in the sectors of basic consumer goods, services, energy transition, and technological innovation.**

India

- **GDP**: The **fastest-growing emerging economy (6.5%),** supported by a **positive demographic factor and public spending on infrastructure** (roads, railways, and airports).
- **Inflation: 4.2%;** marginal annual decline (5.0% in 2024), leading to limited interest rate cuts.
- Market: Elevated valuation multiples; attractive sectors include **financials, technology, and energy transition.**

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IV. Financial Markets

Fixed Income

- Expansive fiscal **measures may be implemented by the Trump administration**, leading to **higher interest rates** and greater volatility across the yield curve, with more pronounced effects on long-term maturities. Additionally, the Federal Reserve is expected to **cut rates more slowly** if inflation risks increase.
- Recommendations:
  - In the U.S.: Focus **on ranges with shorter durations and lower volatility**. Corporate bonds with **investment grade** (IG) due to high credit quality and low default risk, as well as high-yield bonds.
  - European IG Bonds: They offer lower rates with wider spreads **compared to U.S**. bonds and potential appreciation of the EUR vs. USD.
  - Mexican Bonds: **Attractive** due to their **real interest rate**.

Equities

- A **positive outlook** is supported by the extension of the economic cycle in the U.S. and the recovery in Japan. Corporate earnings for the S&P500 are expected to grow **by 15% in 2025 and 13% in 2026.** Additionally, the growth of corporate earnings will be more widespread and driven by artificial intelligence (AI).
- **Attractive Sectors: Finance, medium- and small-sized businesses, electric energy infrastructure, defense, cybersecurity, technology, and companies that integrate AI** to enhance their production processes.
- **Japan**: **Reforms in corporate governance** and exposure to the **technology sector** make it one of the best alternatives.
- **Emerging Markets:** They face significant risks; however, India, with its dynamic economy, represents an **opportunity**. Latin America and **Mexico**, on the other hand, face an uncertain outlook **due to a potential trade war**.

Currencies

- **USD Strength: The USD is expected to remain strong until the expansionary monetary policy cycle concludes.** Concerns about fiscal deficits, government debt, and inflation expectations could put pressure on the USD.
- As the ECB's monetary easing cycle ends and the economy gains more traction, **the EUR is expected to strengthen against the USD**.
- Japan's economic recovery, accompanied by rising interest rates, will support a rebound in the **JPY**.
- Volatility in the MXN could persist during the first half of 2025, potentially exceeding levels of 21.50. **The MXN may stabilize within an average range of 20.00 to 21.50 per USD.**

Alternatives

- **Real Estate** in the U.S.: The real estate sector has strengthened. Investments in **infrastructure and transportation** could provide portfolio stability through **consistent income generation** via REITs and private equity funds.
- A **rebound in mergers and acquisitions activity** is expected in 2025, which will drive capital funds.
- The price of **gold** is anticipated to **surpass the recorded level of USD $2,787.61 per ounce in 2024**, driven by increased demand from central banks.

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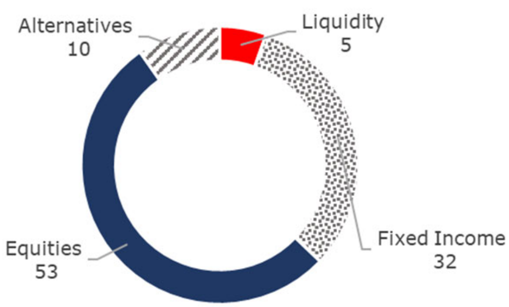
V. Portfolio Strategy

PRIVEST suggests a balanced portfolio structure consisting of 5% in liquidity, 32% in fixed income, 53% in equities, and 10% in alternative instruments.

Chart IV.1 Asset Allocation by Type (%)



- Initially, it will maintain an **allocation of approximately 90% in USD and 10% in MXN.** Liquidity will be managed using government securities in Mexico, as well as other instruments that combine U.S. credit risk with a hedge in MXN.

Fixed Income:

- The bond segment consists of government securities and corporate bonds with **a maximum duration of 3 to 5 years**, aiming to reduce reinvestment risk and avoid high volatility from longer-term instruments.
- **Corporate debt will increase its share in the portfolio composition**.
- **Sovereign bonds from emerging markets** have the potential to add value and profitability, although they carry the risk of USD strength.

Equities:

- The strategy consists of three components: the fundamental portion (Core), tactical or satellite investments, and long-term or thematic positions.
  - Core: Forms the base of the equity strategy, focusing on exposure to **major stock indices**.
  - **Tactics:** Includes participation in emerging and developed markets such as **Japan, India, Taiwan, and Korea**, as well as exposure to **the S&P500 *Equal Weighted*** index due to its valuation discount compared to the original index.
  - **Thematics:** Focuses on **significant trends** expected to transform the economy over the next five years. Key areas include artificial intelligence **(AI) and its enabling infrastructure**, the U.S. financial system, and investments in **both traditional and technological defense sectors**.

Alternatives:

- Portfolios should consider **alternative investments** despite their risk characteristics (volatility, liquidity, term, and concentration), which may not be suitable for all investment profiles. Examples include direct exposure to **real estate investment instruments** and investments in commodities such as gold.

The document is informed through a comprehensive review of literature and analysis of data published by various central banks, international organizations, financial institutions, and economic analysts, all of which are considered reliable sources. While the interpretations and conclusions presented are the author's own, the development of the analysis has been enriched by research and perspectives provided by the following entities.Banco Central Europeo ™, International Monetary Fund ™, World Bank Group ™, Organization for Economic Cooperation and Development ™, Banco de México ™, Federal Reserve Board ™, 日本銀行 Nippon Ginko ™, The Reserve Bank of India ™, Bloomberg L.P. ™, NEW YORKER Marketing & Media International ™, The Economist Newspaper Limited ™, Project Syndicate ™, BlackRock, Inc. ™, The Vanguard Group, Inc. ™, First Trust ™, JPMorgan Chase & Co. ™, Goldman Sachs & Co. ™, Morgan Stanley & Co LLC. ™, Citigroup Inc., Amundi Asset Management, SAS ™, UBS AG ™, Julius Bär Group AG ™, Van Eck Securities Corporation ™, Newsweek Publishing LLC ™, Banco Mercantil del Norte, S.A., Institución de Banca Múltiple, Grupo Financiero Banorte. ™ Banco Ve por Más S.A., Institución de Banca Múltiple, Grupo Financiero Ve por Más ™, Grupo Bursátil Mexicano, S.A. de C.V., Casa de Bolsa.