

2016 Budget proposal – The government keeps its deficit-reduction promise

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- The Minister of Finance delivered yesterday the *Budget proposal for fiscal year 2016* to the Lower House
- This package includes the proposal for the *2016 General Economic Policy Criteria*, the *Revenue Law*, and the *Government Spending Proposal*
- We highlight the following features from the document sent to Congress:
 - (1) The government expects economic growth rates between 2.6% and 3.6% for 2016, an average exchange rate of USD/MXN15.90, an average oil price of US\$50 per barrel, and an a crude oil export platform of 1.1 million barrels per day;
 - (2) The Ministry of Finance (MoF) estimates a 0.2% reduction in revenues, given the significant fall in oil prices;
 - (3) A 2% reduction in public spending, given the 5.9% fall in programmable spending; and
 - (4) A fiscal deficit -ex. Pemex and CFE’s capital spending-, equivalent to 0.5% of GDP in 2016, in line with the MoF’s previous estimate, which will gradually come down to a balanced budget in 2017;

Budget proposal for 2016 – Towards a rational spending budget. We highlight that the *Budget proposal for fiscal year 2016* includes: (1) The so-called *General Economic Policy Criteria* (i.e. the underlying economic assumptions); (2) the proposal for a *Revenue Law*; and (3) the *Government Spending Proposal*. The government assumes that the Mexican economy will grow between 2.6% and 3.6% in 2016, an average exchange rate of USD/MXN15.90, along with a US\$50 per barrel price for the Mexican oil mix. Finally, the MoF considers a 28-day Cetes rate around 4% throughout the year, as shown in the table below.

General Economic Policy Criteria (CGPE) 2016

	CGPE	Consensus*
GDP (% yoy)	2.6 – 3.6	3.0
Inflation	3.0	3.0
USD/MXN (average)	15.90	15.98
Public balance (% GDP)	-3.0	--
Ex. Pemex investments (% GDP)	-0.5	--
Mexican mix of oil (dpb)	50	--

*Banamex’s survey.

Source: SHCP, Banxico and Banorte-Ixe

2016 budget proposal

Bn pesos

	2016	2015	Δ%
Deficit	-577.20	-661.40	-12.7
Revenues	4,137.7	4,146.2	-0.2
Oil revenues	862.8	1,232.7	-30.0
Non-oil revenues	3,274.9	2,913.5	12.4
Spending	4,714.9	4,807.6	-1.9
Programmable	3,530.00	3,751.10	-5.9
Non-programmable	1,184.90	1,056.50	12.2

Source: Ministry of Finance

Lower revenues given lower oil prices. The MoF estimates revenues for 2016 at MXN4.1tn (US\$260.2 bn), which would imply a 0.2% reduction with respect to the expected revenues in 2015. The reduction in expected revenues comes as a result of the lower international oil prices, as shown in the above-mentioned chart. We highlight that the estimated revenues incorporate the *derivatives hedge* made by the Federal Government which warrants an USD\$ 49 income for every oil barrel produced by PEMEX. Moreover, the Oil Stabilization Fund (*FEIP*) will add an additional 3.7 billion pesos (USD\$ 62 bn) which will account for an additional *dollar-per-barrel* (dpb) to Mexico's oil revenue. We highlight that this estimate also incorporates a 12.4% yoy hike in non-oil tax revenues, which attenuates the overall fall in revenues.

Gasoline pricing policy – missing details. The Federal Government also plans to free gasoline prices in order to move towards a liberalized market. However, in 2016 the maximum price will fluctuate given the international reference, but with certain bands –which are still undefined- set to limit its high fluctuations, in order to avoid disorderly price increases that could apply to some market participants in the gasoline's chain production, distribution and marketing. Additionally, it intends to adopt a system of *fixed tax* on fuels, which will not be tied to Pemex operational costs.

Government intends to decrease public spending in around 2% in real terms. Non-discretionary spending will be reduced to 5.9% yoy in real terms with respect to the amount approved for the fiscal budget in 2015. Moreover, discretionary spending will expand 12.9% yoy. In this regard, the Ministry of Education will be assigned more than the 27% of the total programmable spending, which reaffirms the Federal Government's commitment to Mexico's Education Reform.

The government fulfills its goal towards a 0.5% budget deficit in 2016. Moreover, for 2017 the government will achieve a balanced budget (*i.e.* fiscal budget equivalent to 0% of Mexico's GDP). We highlight that this deficit does not include capital investments of government-owned companies (*i.e.* Pemex and CFE) and other projects with high social impact, which is likely to represent about 2.5% of GDP in 2015-2017 coming down to 2% as of 2018.

Sound public finances with realistic assumptions. We believe that the Federal Government’s commitment to reduce its fiscal deficit gradually sends a strong signal to market participants of fiscal responsibility that has characterized the Mexican government since the early nineties especially as this fiscal effort is carried out in an adverse environment of lower oil prices and probable interest rate hikes. We also believe that the assumptions expressed in the *Budget Proposal* are realistic, despite we have a slightly more challenging scenario for GDP growth for 2016 (2.7%), but still within the MoF’s estimated interval (2.6%-3.6%).

What’s next? The Lower House has until October 20 to approve the *Revenue Law* and the *General Economic Policy Criteria*, which will be subsequently turned over to the Senate, who has until October 31 to approve the proposal. We highlight that if any of the two chambers reject the proposal, and the deadline expires, the Executive may request an extension provided that it does not exceed the end of the year, according to the Article 42 of the *Federal Budget and Fiscal Responsibility Law*, and the Article 74 of the *Mexican Constitution*. Once the *Revenue Law* is in place, the Lower House has to approve the spending part of the budget by mid-November, or as already mentioned above, in the case of an extension, the Lower House new deadline will be December 31.

Deadlines for the Budget proposal for 2016

Deadline	
September 8	2016 budget proposal
October 20	Lower House approval of the <i>Revenue Law</i>
October 31	Senate approval of the <i>Revenue Law</i>
November 15	Senate approval of <i>Government Spending Proposal</i>

Source: SHCP

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