

2017 Budget assumptions – Conservative scenario amid a complicated external backdrop

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- The Ministry of Finance (MoF) submitted to Congress its assumptions for 2017 fiscal budget
- The MoF expects a deficit reduction from 3% of GDP to 2.5% in 2017
- This would imply spending cuts of around MXN311.8bn (US\$18.1bn), from which MXN132.3bn (US\$7.7bn) have already been done this year
- Moreover, the government expects a price of the Mexican mix oil in the area of US\$35 per barrel; along with a reduction of the production platform from 2,123mbpd to 2,028mbpd in 2017
- In terms of economic growth, they are forecasting an economic expansion in the range of 2.6% - 3.6% for the next two years; and a USD/MXN17 exchange rate for 2017
- With these assumptions, the Ministry of Finance estimates that the *Historical Balance of the Public Sector Financing Requirements* will start trending downwards in 2017, one year ahead of schedule
- In our opinion, MoF assumptions are yet another evidence of the government's commitment to sound fiscal accounts

Conservative preliminary assumptions for 2017 budget. The Ministry of Finance (MoF) submitted to Congress, according to Article 42 of the *Federal Budget and Fiscal Responsibility Law*, its assumptions for 2017 fiscal budget. In our opinion, MoF made a responsible exercise to face the macroeconomic reality in Mexico, particularly after the sharp fall in oil prices and their likely persistence at low levels, as well as the high volatility in global financial markets.

Additional spending cut to comply with deficit target. The Ministry of Finance maintained its objective to reduce public deficit from 3% of GDP in 2016 to 2.5% next year. This implies a spending cut amounting to MXN311.8bn (US\$18.1bn), which MXN132.3bn (US\$7.7bn) was already implemented this year, so the cut in 2017 will be only MXN175.1bn (US\$10.2bn). In this context, the MoF expects lower budget revenues and an increased non-programmable spending by MXN93.7bn (US\$5.4bn). Additionally, the Ministry of Finance estimated budget revenues by MXN4.2tn (US\$242.7bn) for 2017 and net spending of MXN4.7tn (US\$272.4bn), which are 2.8% and 4.2% respectively lower than the amount expected in 2016.

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Deficit reduction based on conservative assumptions. MoF's assumptions do not include the use of extraordinary revenues such as operational Banxico's surplus expected to be announced this week. In this context, the main factor impacting the budget revenues estimates for 2017 will come from low oil revenues, on the back of lower levels of production (2,123mbpd vs. 2,028mbpd) and prices (US\$35 per barrel vs. US\$49 per barrel in 2016).

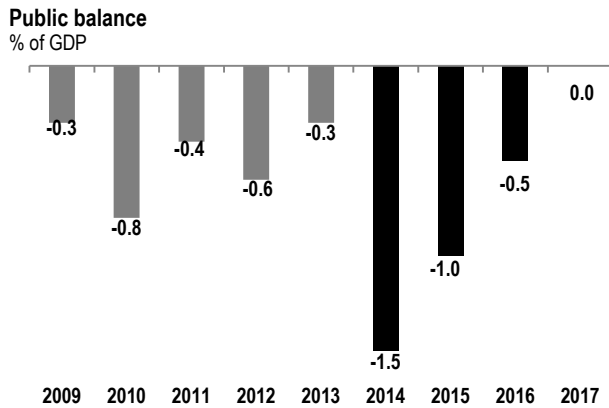
The MoF expects an economic expansion between 2.6% to 3.6% in the next two years. The estimated for Mexico's economic growth this year was unchanged in a range between 2.6% and 3.6%, while the MoF posted a similar growth forecast for 2017 to a range between 2.6% and 3.6%. Moreover, the exchange rate for 2017 is estimated at USD/MXN17, while the inflation estimate for 2016 and 2017 is at 3%, as shown in the following table.

Ministry of Finance economy overview 2016 – 2017

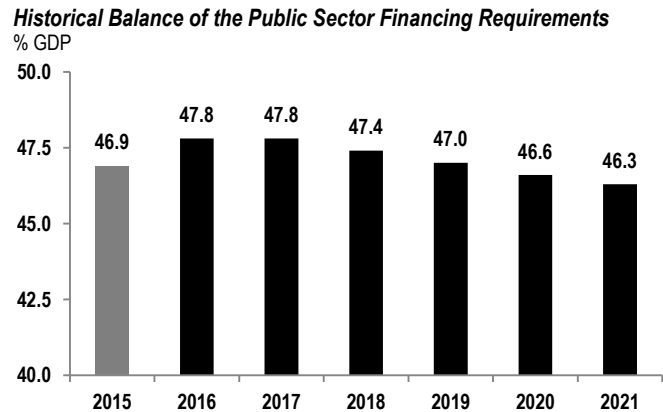
	2016e	2017e
GDP		
%; GDP–real growth rate (range)	2.6 – 3.6	2.6 – 3.6
Nominal (billions of pesos)	19,203.9	20,432.4
GDP deflator	3.2	3.3
Inflation		
December / December	3.0	3.0
Nominal exchange rate		
End of period	17.5	17.0
Average	18.0	17.2
Interest rate (CETES 28 días)		
% Nominal end of period	4.3	5.3
% Nominal average	3.7	4.8
% Actual cumulative	0.8	1.8
Current account balance		
Millions of dollars	-33,067.8	-34,429.8
% of GDP	-3.1	-2.9
Fiscal balance (% of GDP)		
With inversion	-3.0	-2.5
Without inversion	-0.5	0.0
Mexican petroleum		
Average price (dpb)	25	35
Average production platform	2,123	2,028
Average export platform	968	873

Source: SHCP
e = estimate data

With these assumptions, the Ministry of Finance estimates that the *Historical Balance of the Public Sector Financing Requirements* will start trending downwards in 2017, one year ahead of schedule. It is consistent with the fiscal consolidation effort that the government has done. According to the MoF, Mexico’s government has the tools to make adjustments without damaging the economic growth and maintains a commitment to not increase public debt or raise taxes.



Source: MoF



Source: MoF

Commitment with sound fiscal accounts. In our opinion, MoF assumptions denote a clear commitment towards reducing fiscal deficit at the end of this administration (2018), notwithstanding the adverse external backdrop and the difficult financial situation of Pemex, in the absence of more taxes, adjusting to external shocks of the persistence of lower oil prices and the potentially higher costs of short-term financing, and lower oil production platform.

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