

AMLO's landslide victory in historical Presidential election – What's next?

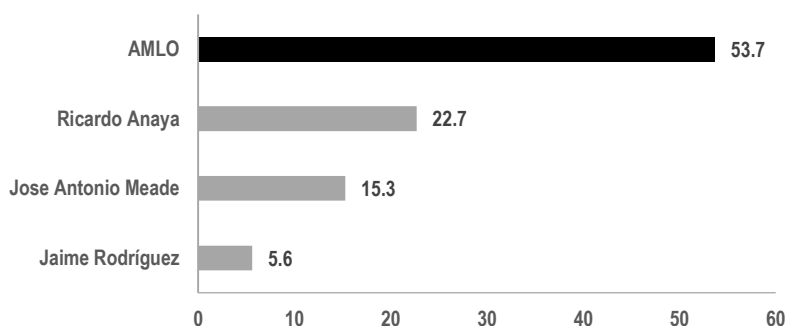
July 2, 2018

www.banorte.com
@ analisis_fundam

- **Andrés-Manuel López-Obrador (AMLO) won Mexico's Presidential election in a landslide victory with 53.7% of the votes, considering 44.4% of the ballots**
- **Moreover, it is highly likely that AMLO's party, Morena, could get simple majority (i.e. more than 50%) in both chambers, but not enough to perform constitutional changes (i.e. more than 66.6%)**
- **It is our take that the new government will keep Mexico's strong macroeconomic framework, with fiscal responsibility and a deep respect towards central bank independence -among others-, as he highlighted in his first message as virtual president elect, last night**
- **As we have noted earlier, we continue to anticipate that the rally that we have observed in the past few days in local financial assets will continue, including the peso vis-à-vis the US dollar**

AMLO, virtual president-elect of Mexico. In line with what polls suggested, Andrés-Manuel López-Obrador (AMLO), won the presidential election by a large majority. In this context, we believe that the risk of a post-election conflict is negligible since all the candidates have already recognized AMLO's victory. In fact, with 44.4% of the computed ballots (according to the PREP), AMLO obtained 53.7% of the votes, followed by Ricardo Anaya (22.7%), Jose-Antonio Meade (15.3%) and, in a distant fourth place, Jaime Rodríguez "El Bronco" (5.6%), as observed in the chart below.

Electoral results with vote count at 1.6%
% of votes



Source: PREP

Main economic indicators

	2017	2018 f
GDP (% yoy)	2.0	2.5
Inflation (% yoy, end of period)	6.8	4.3
FX (USD/MXN, end of period)	19.74	18.60
Public balance (as measured by the PSBR, % of GDP)	-1.1	-2.5
Public debt (as measured by the HBPSBR, % of GDP)	46.0	45.5
Debt duration (years)	6.1	6.3
Current account balance (% of GDP)	-1.7	-1.8
FDI (US\$ bn)	30.3	30.2
Stock market valuation (times, FV/EBITDA)	9.3x	8.9x

Source: INEGI, Banxico, Ministry of Economy, Bloomberg and Banorte

Mexico's credit ratings

	Rating	Outlook
S&P	BBB+	Stable
Fitch Ratings	BBB+	Stable
Moody's	A3	Stable

Source: Rating agencies and Bloomberg

Gabriel Casillas

Chief Economist and Head of Research
gabriel.casillas@banorte.com

Delia Paredes

Executive Director of Economic Analysis
delia.paredes@banorte.com

Alejandro Padilla

Head Strategist - Fixed-Income and FX
alejandro.padilla@banorte.com

Manuel Jiménez

Head Equity Research
manuel.jimenez@banorte.com

Tania Abdul

Head Corporate Debt
tania.abdul@banorte.com

CONFERENCE CALL WITH CARLOS URZUA

Time: 9:00am ET
Dial in: +1 786 2336715
ID: 575012

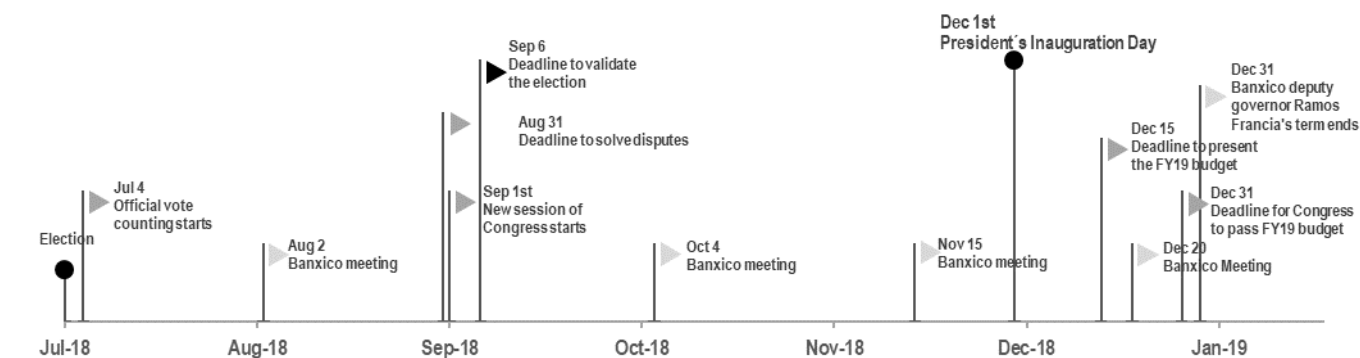
Document for distribution among public

Legislative majority, but not enough for constitutional amendments. Voting trends in the congressional election suggest that the party of the new president, *Morena*, will obtain a simple majority (*i.e.* more than 51%) in both houses. Nevertheless, it will not have the super-majority (66.6% of the seats) needed to amend the constitution, and therefore change the recently-approved structural reforms. It is also worth noting that an additional condition to modify the constitution has to do with local congresses. In this context, we will pay close attention to the outcome of these elections as well. For a constitutional amendment to be approved, it needs two thirds of both Federal houses, plus half of local congresses (16 out of 32).

Sound macroeconomic fundamentals will be maintained. In our view, the new government will maintain sound macroeconomic fundamentals. In fact, in his first message as virtual president elect, López-Obrador stated that he will keep a fiscally-responsible policy, following Mexico’s current fiscal consolidation process -with no need to increase taxes or public debt-, and paying deep respect towards central bank independence, among others. In his speech AMLO highlighted he said that energy contracts will be reviewed to check for possible corrupt behavior.

What’s next within the electoral process? In the next few days, the official count will start, which will finally legally validate election. This calculation will begin on July 4th and the *National Electoral Institute* (INE) has until September 6th to validate it. Among the key dates for the remainder of the year, in terms of the political transition, is the inauguration of the new Congress on September 1st; the inauguration of the new president on December 1st, as well as the FY2019 budget, which will be processed in the last month of the year (see timeline below)

Timeline of main events after the 2018 election



Fuente: Banorte

Macroeconomic perspectives 2018-2019. We maintain our expectation for a GDP expansion of around 2.5% in 2018 with inflation ending the year at 4.3% while for year-end 2019 we expect inflation at 3.5%. In addition, we expect Banxico to remain on hold with the reference rate at 7.75% over the next 18 months.

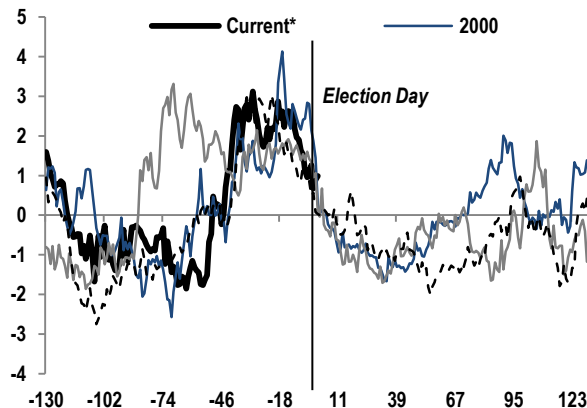
NAFTA and AMLO. It is worth mentioning that this election takes place mid the uncertainty generated by the renegotiation of NAFTA and protectionist policies by President Trump's administration. It is worth noting that Mr. López-Obrador nominated Jesús Seade, former negotiator of the original NAFTA, who held high-level positions at both the World Bank and the WTO, as his main NAFTA re-negotiator. It is also worth noting that President Trump said yesterday that he will not sign any agreement until after the U.S. mid-term elections, which will take place in November. In our opinion, we expect continuity in Mexico's negotiating position on this issue and we continue to expect that it will be favorable.

We expect the pre-electoral rally will continue in the post-electoral world.

The peso initially reacted to the preliminary results with a modest rally of 1.4% moving from USD/MXN 19.91 to 19.64, however it has pulled back to the 20.00 area following the sell-off in emerging markets. In our view, market participants will focus on the details inside the proposed economic policies from the President-elect and his team during the transition process. His comments suggesting fiscal consolidation and continuity of the current strategy when negotiating NAFTA terms with the U.S. and Canada and other key aspects of the economy (*e.g.* honoring the independence of the central bank) makes us believe that a post-electoral rally will take place in the 2H18, in a similar fashion as in the previous electoral processes as depicted in the RHS chart below. We expect the performance of interest rates to portray a performance alike, with country risk premia possibly portraying a stable macroeconomic framework. In addition, the narrow trading range of the Mexican peso in the aftermath of the results suggests that the market has priced in an AMLO victory. Nevertheless, in our view market participants did not anticipate that his party, Morena, could obtain majority in both chambers. In our view, this new information could result in a more limited short-term rally, conditioned to a market friendly message from AMLO and his cabinet. In this regard, today's likely MoF, Carlos Urzúa, will have a conference call with investors in English at 9:00am ET (+1-786 233-6715, ID: 575012). With a mid-term horizon we expect the pre-electoral rally to continue in the post-electoral world. In terms of strategy, we stay without directional positions in USD/MXN as the current level is not attractive enough as an entry for short positions, which would we suggest at or above 21.00 per dollar. Nevertheless, we favor this bias for trading and risk-tolerant investors as uncertainty dissipates and NAFTA negotiations resume with a more favorable valuation and cleaner positioning, seeing the possibility of a gradual shift towards a critical support at 19.00 per dollar this month.

USD/MXN: Z-score during Presidential Elections

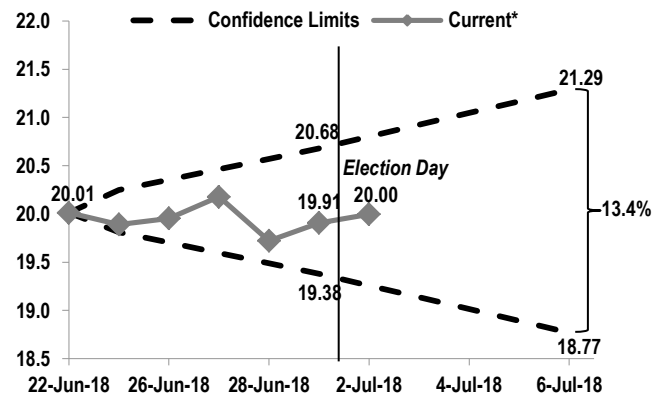
In standard deviations relative to the 90-day MA, based on daily data
(unit)



* Closing prices except for July 2, 2018, which is the last trading level as of 7:15am (EST)
Source: Banorte with data from Bloomberg

USD/MXN: 90% Confidence interval

Pesos per dollar, based on short-term ATM options as of Jun/22/18
(unit)

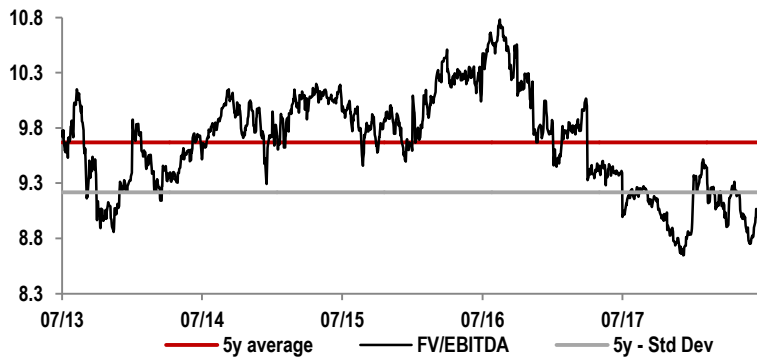


* Closing prices except for July 2, 2018, which is the last trading level as of 7:15am (EST)
Source: Banorte with data from Bloomberg

Stock market strategy. During the last months, the benchmark index of the Mexican Stock Exchange (IPC) has been highly volatile, mainly due to: (1) International geopolitical risks; (2) uncertainty regarding NAFTA negotiations; (3) the interest rates normalization of the Federal Reserve; and (4) the elections in Mexico. As such, risk aversion drove a sell-off for Mexican stocks and the IPC index de-rated. In this context, as of the end of May, the IPC reached a 12-month low of 44,662pts, trading at 8.8x FV/EBITDA. In June, the benchmark bounced back by 3,000pts, or a 6.7% m/m rise, as investors saw bargains, triggering a re-rating towards 9.1x. Current valuation implies a 5.6% discount against its five-year historical average.

Given the results of the election process, we expect a positive reaction for the IPC index, as some of its constituents are trading at attractive valuations, and the uncertainty surrounding the election has been dispelled. In our view, the benchmark could move towards the 49,000pts (9.3x FV/EBITDA) level in the following days, to trade in line with its historical averages. Nonetheless, we do not rule out the possibility of experiencing some periods of volatility. Either way, investors should remain cautious, as long as uncertainty regarding NAFTA negotiations and global trade conflicts remain on the loop. We believe that our Equity Strategy exemplifies an appropriate diversification, by being integrated by companies with strong fundamentals, high marketability and a positive outlook.

Stock Market Valuation
FV/EBITDA 2013-2018

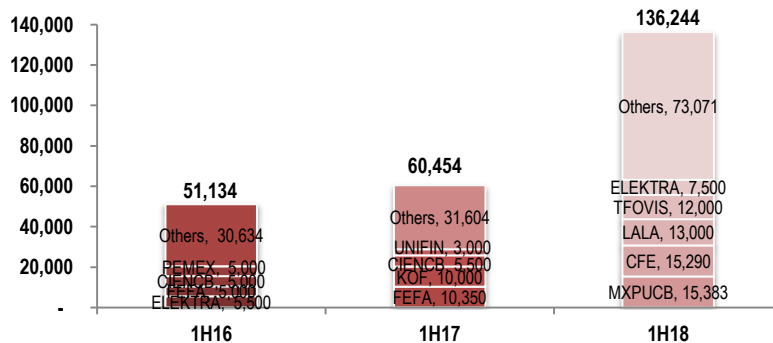


Source: Banorte, Bloomberg

Corporate bond issuers covered their financing needs in 1H18. As of the first half of 2018, the medium and long-term corporate market showed a great dynamism with a placed amount of MXN 136,244 million (USD 6.8 billion), 1.25x and 1.66x higher than the amount issued during the first half of 2017 (MXN 60,454 million, USD 3.0 billion) and 2016 (MXN 51,134 million, USD 2.5 billion), respectively. Likewise, for the last 12 months (July 2017 to June 2018) the amount placed totaled MXN 304,876 million, (USD 15.2 billion) which is 33% higher than the amount issued during 2017. This growth was spurred by the issuers and investors funding their needs before the 2018 election. In the short term, we expect a lower activity (issuances) focusing on refinancing and working capital needs (short term debt).

Amount issued 1H16 / 1H17 / 1H18

\$mop



Source: Banorte / BMV / Valmer, with information as of June 2018.

Winners of state governorships

%, results interval according to each states "fast count"

State	Winner	% of votes
Chiapas	Rutilio Cruz Escandón (Morena, PT, and PES)	40.2 – 44.2
Ciudad de México	Claudia Sheinbaum (Morena, PT, and PES)	46.6 - 47.7
Guanajuato	Diego Sinhué Rodríguez (PAN, PRD, and MC)	49.5 – 51.5
Jalisco	Enrique Alfaro Ramírez (MC)	37.7 – 40
Morelos	Cuauhtémoc Blanco (Morena, PT and PES)	51.0 – 53.8
Puebla	Non-definitive confidence intervals between Martha Érika Alonso (PAN, PRD, and MC) and Miguel Barbosa (Morena, PT, and PES)	
Tabasco	Adán Augusto López (Morena, PT, and PES)	62.1 – 64.3
Veracruz	Cuitláhuac García Jiménez (Morena, PT, and PES)	43.9 – 45.9
Yucatán	Mauricio Vila Dosal (PAN and MC)	38.0 -40.8

Source: INE, State electoral institutes

Disclaimer

The information contained in this document is illustrative and informative so it should not be considered as an advice and/or recommendation of any kind. BANORTE is not part of any party or political trend.

GRUPO FINANCIERO BANORTE S.A.B. de C.V.
Research and Strategy

Gabriel Casillas Olvera	Chief Economist and Head of Research	gabriel.casillas@banorte.com	(55) 4433 - 4695
Raquel Vázquez Godínez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967

Economic Analysis

Delia María Paredes Mier	Executive Director of Economic Analysis	delia.paredes@banorte.com	(55) 5268 - 1694
Katia Celina Goya Ostos	Senior, Global Economist	katia.goya@banorte.com	(55) 1670 - 1821
Miguel Alejandro Calvo Domínguez	Economist, Regional	miguel.calvo@banorte.com	(55) 1670 - 2220
Francisco José Flores Serrano	Economist, Mexico	francisco.flores.serrano@banorte.com	(55) 1670 - 2957
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611

Fixed income and FX Strategy

Alejandro Padilla Santana	Head Strategist – Fixed income and FX	alejandro.padilla@banorte.com	(55) 1103 - 4043
Juan Carlos Alderete Macal, CFA	FX Senior Strategist	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Santiago Leal Singer	Strategist Fixed income and FX	santiago.leal@banorte.com	(55) 1670 - 2144

Equity Strategy

Manuel Jiménez Zaldivar	Director Equity Research — Telecommunications / Media	manuel.jimenez@banorte.com	(55) 5268 - 1671
Victor Hugo Cortes Castro	Equity Research Analyst	victorh.cortes@banorte.com	(55) 1670 - 1800
Marissa Garza Ostos	Senior Equity Research Analyst – Conglomerates / Financials/ Mining / Chemistry	marissa.garza@banorte.com	(55) 1670 - 1719
José Itzamna Espitia Hernández	Equity Research Analyst – Airlines / Airports / Cement / Infrastructure / Fibras	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Equity Research Analyst – Auto Parts/ Consumer Discretionary / Real Estate / Retail	valentin.mendoza@banorte.com	(55) 1670 - 2250
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@banorte.com	(55) 1670 - 2251

Corporate Debt

Tania Abdul Massih Jacobo	Director Corporate Debt	tania.abdul@banorte.com	(55) 5268 - 1672
Hugo Armando Gómez Solís	Senior, Corporate Debt	hugo.gomez@banorte.com	(55) 1670 - 2247
Gerardo Daniel Valle Trujillo	Analyst, Corporate Debt	gerardo.valle.trujillo@banorte.com	(55) 1670 - 2248

Wholesale Banking

Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(55) 1670 - 1889
Alejandro Eric Faesi Puente	Head of Global Markets and Institutional Sales	alejandro.faesi@banorte.com	(55) 5268 - 1640
Alejandro Aguilar Ceballos	Head of Asset Management	alejandro.aguilar.cebillos@banorte.com	(55) 5268 - 9996
Arturo Monroy Ballesteros	Head of Investment Banking and Structured Finance	arturo.monroy.ballesteros@banorte.com	(55) 5004 - 1002
Gerardo Zamora Nanez	Head of Transactional Banking, Leasing and Factoring	gerardo.zamora@banorte.com	(81) 8318 - 5071
Jorge de la Vega Grajales	Head of Government Banking	jorge.delavega@banorte.com	(55) 5004 - 5121
Luis Pietrini Sheridan	Head of Private Banking	luis.pietrini@banorte.com	(55) 5004 - 1453
René Gerardo Pimentel Ibarrola	Head of Asset Management	pimentelr@banorte.com	(55) 5268 - 9004
Ricardo Velázquez Rodríguez	Head of International Banking	rvelazquez@banorte.com	(55) 5004 - 5279
Victor Antonio Roldan Ferrer	Head of Corporate Banking	victor.roldan.ferrer@banorte.com	(55) 5004 - 1454