

July: Mexico confirms external accounts strength and economic stagnation

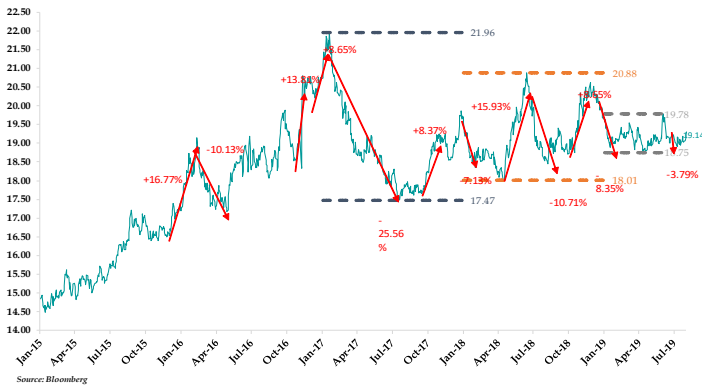
Data released in July confirmed the strength of Mexico's external accounts but, also, an economic stagnation. Mexbol was not able to support the economic deceleration, and 2Q19 earning reports confirmed it. Besides, the Index was also hampered by increased systematic risk resulting from the trade conflicts between China and the United States.

Exchange Rate

The spot exchange rate was not able to support the volatility and a strengthening U.S. dollar; however, the peso appreciated 0.42% month-over-month (MoM), leaving year-to-date appreciation as of July 31st at 2.6%.

Noteworthy, the Mexican peso is the second currency that has appreciated the most in the year, only after the Canadian dollar, and explained by the strength of its external accounts. In the first half of the year, Mexico consolidated as the leading U.S. commercial partner, with a substantial surplus, which may increase if the new tariff announced by Trump materializes. Also, accumulated remittances to July again reached all-time highs.

**Spot Exchange Rate MXN/USD
 (As of July 31st, 2019)**



Mexican Stock Exchange

July represented the worst month of the year so far for Mexbol as the poor performance of the index was aggravated in the last three weeks. Mexbol closed the month at 39,977, a monthly decline of (-) 5.15% and leading to a slight year to date return of 0.17%. The drop of the index reflects general despair in international markets, and the confirmation of economic stagnation in Mexico in the first half of 2019. Besides, the market did not respond well to the rescue plan proposed by the Ministry of Finance to reactivate the economy, as it considered it faulty.

10 Year Bonds

In the face of new tariff threats to China and increased market volatility, international investors sought refuge in safer assets such as the US Treasuries. The 10-year Treasury yield plunged 29 basis points to 1.70% while the 10-year M-bond fell to 7.46%, a weekly drop of 7 basis points and offering one of the highest yields within emerging markets.

**10-Year M Bond
 (As of July 31st, 2019)**



Ministry of Finance Decisions

a. Economic Reactivation Program

The Ministry of Finance announced a program to reactivate the economy, which consists of an injection of approximately US\$25 billion, distributed as follows:

- I. US\$14 billion, 56% of the total, destined to Development Banks to offer credits and guarantees up to 500 thousand micro, small and medium companies.
- II. US\$6 billion, 23.95% of the total, destined to the public sector. Specifically, to bring 2020 programmed public tenders forward and to government hiring for this year.
- III. US\$2.5 billion, 10.41% of the total, will be used for infrastructure. A total of 18 projects will be built with private and public funding; 80% and 20% respectively.
- IV. US\$2.5 billion, 10.41% of the total, allocated to Mexico's agricultural sector through credits.

Although the US\$25 billion seems significant as it is equivalent to 2.04% of 2018 nominal GDP, the program has the following deficiencies:

- i. The amount of liquid resources, which consists of US\$6 billion in government spending plus US\$2.5 billion in infrastructure, represents only 0.7% of GDP.
- ii. The liquid resources mentioned above only represent 95% of what the government has stopped spending in 2019, so they are not enough to compensate for this situation.
- iii. The credit program is ambitious; however, it lacks calendarization and generates doubts as to the quality of the credits.

b. Public Finances Quarterly Report

The Ministry of Finance presented the report on public finances for the first half of the year. The primary balance was US\$11.83 billion, 168.4% higher than the budgeted at the beginning of the year. The above is not a consequence of an increase in income since these were 2.54% lower than those scheduled (US\$139.4 million). What allows the Ministry of Finance to meet its 1.0% GDP primary surplus goal is the sub-exercise of spending, which during the first half of the year amounts to US\$9.05 billion, 5.91% less than budgeted.

c. Liability Management by the Ministry of Finance

The Ministry of Finance (SHCP) announced a maturity improvement operation in international markets for US\$3,560 million, within the limits of the external indebtedness established in the 2019 Economic Package.

The resources to finance this operation were obtained through the reopening of the dollar-denominated bond with maturity in April 2029 and a coupon rate of 4.5% for a total amount of US\$1,456 million; and by issuing a new 30-year reference bond with maturity in 2050 with a 4.5% coupon rate for a total amount of US\$2,104 million. The transaction reached a maximum demand of US\$9.5 billion (2.6 times the amount placed).

The Ministry of Finance carried out the operation as follows:

1. Withdrawal of a dollar-denominated bond due in January 2021 for a total of US\$933 million.
2. Exchange of outstanding bonds denominated in dollars with maturities in both the short part (2019-2026) and the long part (2031-2047) of the yield curve for approximately US\$2,456 million.

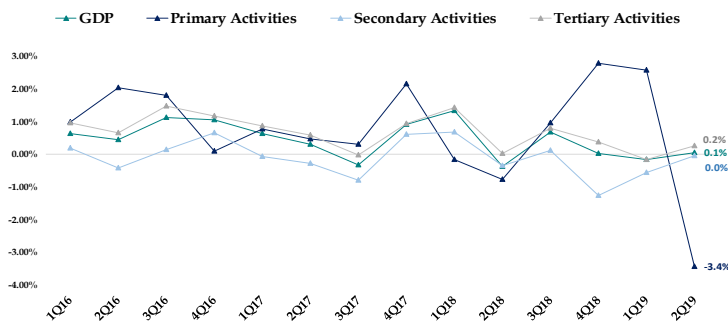
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Economic Indicators

Gross Domestic Product Estimation

The National Institute of Statistics and Geography (INEGI) announced that the Gross Domestic Product (GDP) for 2Q19 grew 0.1% quarter-over-quarter (QoQ), compared to a negative figure expected by market consensus which would have hauled a technical recession. On an annual basis, GDP grew 0.4% and exhibited the stagnation of the Mexican economy. By components, primary activities (agriculture, forestry, and fishing) and services (which represent around 60% of GDP) expanded by 1.7% and 1% respectively while the industrial activity (manufacturing, construction, mining, and commodities) contracted by -1.6%.

Quarterly GDP by Component
 Year over year Growth



Source: INEGI

PEMEX 2019-2023 Business Plan

The 221-page document develops a strategy in which the Government of Mexico will make considerable investments to stabilize Pemex's finances in the next three years (2019-2021). Afterward, the government expects that in the following years (2022-2023) the parastatal will once again become a driver of development for the country. From 2019 to 2023, the total investment of the government will amount to approximately US\$11,854 million; this amount is equivalent to 25% of the total investment that Pemex will make in the same period. Moreover, it distributes as follows:

- 52% of the Mexican Government investment (approximately US\$ 6,164 million taking into consideration an exchange rate of 19.06 pesos per dollar) will be capital injections that government will deliver within three years; US\$ 3,461 million for 2019, US\$1,993 million for 2020, and US \$1,940 for 2021.
- The remaining 48% (US\$ 5,690 million) will be delivered to the oil company through a decrease in the tax burden. Specifically, with the reduction from 65% to 54% of the tax rate of the Right to Shared Profit (DUC). The change will be gradual and will begin with a decrease to 58% in 2020 and the second adjustment to 54% in 2021.

Trade Balance

The trade balance in June presented a surplus of US\$2,561 million and compared positively with the deficit of US\$899 million in the same month of 2018. Year to date, the trade surplus amounts \$ 3,145. Merchandise exports in the first sixth months of the year totaled US\$37,949 million, comprised of US\$35,951 million in non-oil exports and US\$1,998 million of oil exports. Thus, in June, exports increased 1.2% year-to-date driven by a 2.8% increase in non-oil exports and a drop of (-) 20.4% in oil exports. Merchandise imports amounted US\$35,388 million; this represents a monthly variation of (-) 6.3% for non-oil imports and (-) 18.6% for oil imports.

Exports									
	2018	% of Total	Annual Change	2019 YTD	% of Total	Annual Change	Jun-19	% of Total	Annual Change
Total Exports	430,655	100.0%	40.1%	227,273	100.0%	3.7%	37,949	100%	1.2%
Oil	30,601	6.8%	26.86%	13,852	6.1%	-9.5%	1,998	5.3%	-20.4%
Crude Oil	26,512	5.9%	32.25%	12,139	5.3%	-7.6%	1,741	4.6%	-19.0%
Others	4,089	0.9%	11.16%	1,742	0.8%	-20.7%	257	0.7%	-26.5%
Non-Oil	420,053	93.2%	39.1%	213,392	93.9%	4.7%	35,951	94.7%	2.6%
Agricultural	16,505	3.7%	31.7%	9,705	4.3%	-4.1%	1,304	3.4%	4.9%
Mining	6,232	1.4%	14.03%	3,024	1.3%	-5.3%	506	1.3%	-7.3%
Manufacturing	397,344	92.2%	9.0%	200,663	88.3%	-4.7%	34,141	90.0%	2.9%
Automotive Industry	142,178	33.0%	12.24%	72,575	31.9%	6.2%	12,581	33.2%	4.4%
Others	235,165	54.6%	7.5%	128,088	56.4%	4.2%	21,560	56.5%	2.0%
Imports									
	2018	% of Total	Annual Change	2019 YTD	% of Total	Annual Change	Jun-19	% of Total	Annual Change
Total Imports	464,302	100.0%	40.4%	224,125	100%	0.2%	35,388	100%	-7.6%
Oil	53,782	11.6%	28.4%	24,467	10.9%	-4.4%	3,830	10.8%	-18.6%
Non-Oil	410,541	88.4%	7.9%	199,661	89.1%	0.6%	31,559	89.2%	-6.3%
Consumption Goods	43,616	9.4%	3.1%	20,379	9.1%	-1.7%	3,204	9.1%	-5.7%
Intermediate Goods	321,037	69.1%	8.0%	158,776	70.5%	2.0%	25,347	71.6%	-4.2%
Capital Goods	45,887	9.9%	11.9%	20,505	9.1%	-5.0%	3,005	8.5%	-21.2%
Trade Balance									
	2018	2019 YTD	Annual Change	Jun-19	Annual Change				
Trade Balance	-13,647	3,145	N.D.	2,561	41.9%				

Source: Mexico's Ministry of Economics
 Amounts in Millions of Dollars

United States International Trade Balance

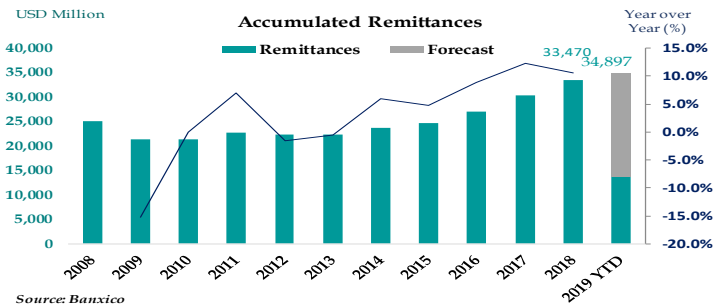
For the sixth consecutive month, in June, Mexico once again was the leading trading partner of the United States. Total trade between the two countries amounted to more than US\$311 billion, representing 14.9% of US total trade; the year to date surplus amounts to US\$49.6 billion. Mexico has been the most benefited country from the trade tensions between the United States and China; in the face of President Trump's new tariff threat, Mexico's position as the leading trading partner strengthens.

United States International Trade (As of June 2019)				
Country	Exports	Imports	Total Trade	Balance
Mexico	130,930	180,531	311,461	-49,601
% of Total	15.8%	14.3%	14.9%	
Canada	147,746	157,837	305,583	-10,091
% of Total	17.8%	12.5%	14.6%	
China	54,937	234,751	289,688	-179,814
% of Total	6.6%	18.6%	13.0%	
Japan	37,320	73,840	111,160	-36,520
% of Total	4.5%	5.9%	5.3%	
Germany	30,028	63,450	93,478	-33,422
% of Total	3.6%	5.0%	4.5%	
Korea, South	27,949	39,210	67,159	-11,261
% of Total	3.4%	3.1%	3.2%	
United Kingdom	33,368	31,423	64,791	1,945
% of Total	4.0%	2.5%	3.1%	
France	19,318	30,416	49,734	-11,098
% of Total	2.3%	2.4%	2.4%	
Country Exports Imports Total Trade Balance				
India	18,624	29,433	48,077	-10,829
% of Total	2.2%	2.3%	2.3%	
Taiwan	15,744	26,676	42,420	-10,932
% of Total	1.9%	2.1%	2.0%	
Italy	11,607	28,491	40,098	-16,884
% of Total	1.4%	2.3%	1.9%	
Brazil	21,509	16,225	37,734	5,284
% of Total	2.6%	1.3%	1.6%	
Singapore	15,364	13,599	28,963	1,765
% of Total	1.9%	1.1%	1.4%	
Hong Kong	16,132	2,200	18,332	13,932
% of Total	1.9%	0.2%	0.9%	
Saudi Arabia	7,166	7,829	14,995	-663
% of Total	0.9%	0.6%	0.7%	
All other countries	240,814	323,171	563,985	-82,357
% of Total	29.1%	25.7%	27.0%	
TOTAL 2019 YTD	828,556	1,259,102	2,087,658	-430,546
TOTAL 2018	1,664,064	2,542,735	4,206,799	-878,671
TOTAL 2017	1,546,654	2,342,905	3,889,559	-796,251

Source: U.S. Census Bureau
 Amounts in millions of dollars

Remittances

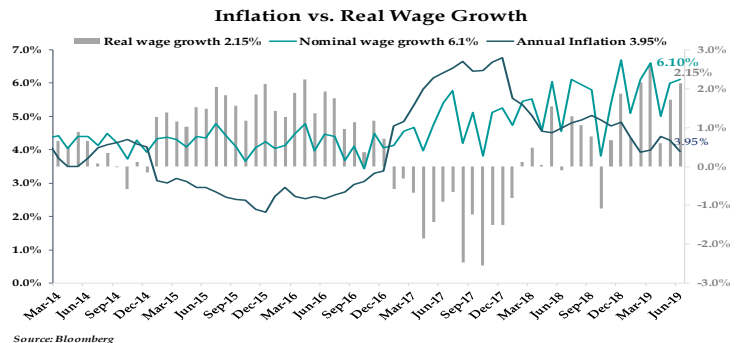
Remittances in June amounted US\$3.11 billion and accumulated US\$16.84 billion year-to-date, 3.7% higher compared to June 2018, and the highest in history. With this data, the flow of remittances observed this year is reaffirmed and is heading for a record US\$35 billion in 2019.



Source: Banxico

Wages and Inflation

Contractual wages in June registered a 6.5% YoY increase; if compared to the 3.95% annual inflation rate, real wages have increased by 2.15%. Since the beginning of the year, remunerations have been altered due to the 16% increase in the minimum wage, driving higher costs for companies while the Global Labor Productivity Index of the Economy (IGLPIE) presented a 0.5% YoY decrease in 1Q19; this generates resistance to a lower inflation rate due to the rigidity of the labor market. Under this argument, several members of the Governing Board of Banxico are reluctant to reduce the reference rate shortly.



Source: Bloomberg

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Compliance & Portfolio Administration

Definitions

Banco de Mexico (Banxico): Mexico Central Bank, lender authority and lender of last resort.

Basis point: One basis point is equal to 1/100th of 1%, or 0.01%, or 0.0001.

Gross Domestic Product: a monetary measure of the market value of all the final goods and services produced in a period of time, often annually.

MEXBOL : The S&P/BMV IPC Index measures the performance of the largest and most liquid stocks listed on the Bolsa Mexicana de Valores. The index is designed to provide a broad and representative index covering the Mexican equities market. It is not possible to invest directly in an index.

Balance of Payments: the record of all economic transactions between the residents of a country and the rest of the world.

Trade Balance: the difference between the value of imports and exports.

Same Store Sales: total dollar amount of sales in stores that have been operating for a year or more.

Ceteris paribus: A Latin expression meaning other things remaining the same.

PEMEX: Petróleos Mexicanos, which translates to Mexican Petroleum, is the Mexican state-owned petroleum company, created in 1938 by nationalization or expropriation of all private, foreign, and domestic oil companies at that time. The Fund maintains 0.0% investment in the security, at the close of July 31, 2019. For a list of full securities please visit: www.mxefund.com.

Global Indicator of Economic Activity: The Global Indicator of Economic Activity allows to know and monitor the monthly evolution of the real sector of the economy..

INEGI - The National Institute of Statistics and Geography. It is the institution responsible for performing the population census every ten years; as well as the economic census every five years and the agricultural, livestock and forestry census of the country.

Spot Exchange Rate: Is the current price level in the market to directly exchange one currency for another, for delivery on the earliest possible value date. Cash delivery for spot currency transactions is usually the standard settlement date of two business days after the transaction date (T+2)..

Disclosures

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