Fiscal Stability Monitor

May 14, 2020

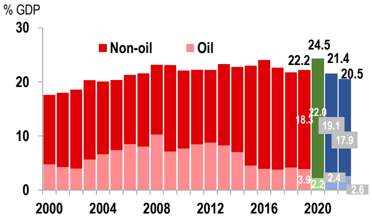
www.banorte.com
@analisis_fundam

Delia Paredes
Executive Director of Economic Studies
delia.paredesl@banorte.com

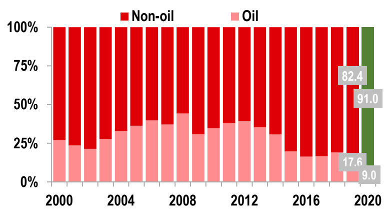
- **Fiscal sustainability is one of the main fundamentals for macroeconomic stability of a country. This has been the case of the Mexican economy for at least the last 20 years**
- **The Mexican government is required by law to maintain a balanced budget. In this context, the definition of public sector balance excludes investment of the government in Pemex and CFE, mainly, which is, in turn, accounted for in the *Public Sector Borrowing Requirements***
- **In addition, stabilization funds were created in order to apply countercyclical fiscal policy when needed**
- **In terms of revenues, it is worth noting that the federal government has gradually reduced its dependence on oil revenues**
- **Stability in the levels of income tax and VAT collection, as a percentage of the GDP, denotes its procyclical nature**
- **Programmable spending has been reduced. However, this has been done at the expense of capital spending**
- **Dynamics of spending on pensions represent an increasing percentage of GDP, while federalized spending remains relatively constant**

Historical series | Year to date | Target in CGPE*

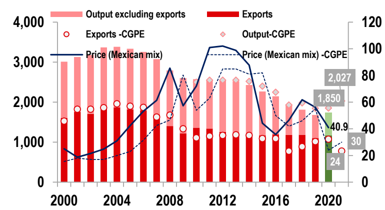
Budget Revenues
% GDP



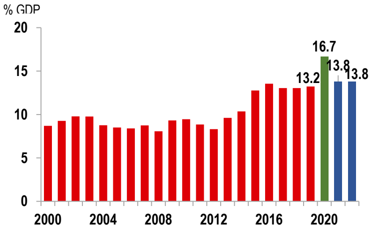
Composition of budget revenues
% total



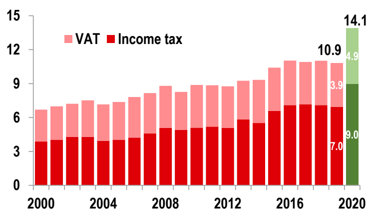
Output, exports & oil prices
mbd (lhs), dpb (rhs)



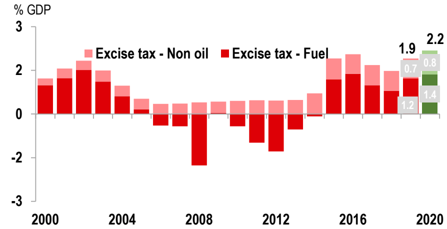
Non-oil tax revenues
% GDP



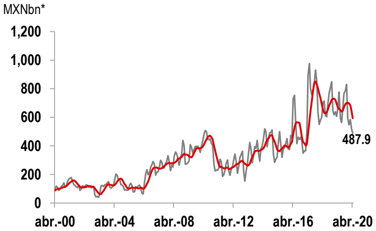
Tax revenues - Income tax & VAT
% GDP



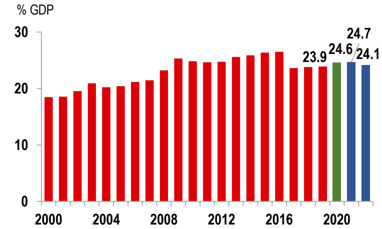
Tax revenues - Excise taxes
% GDP



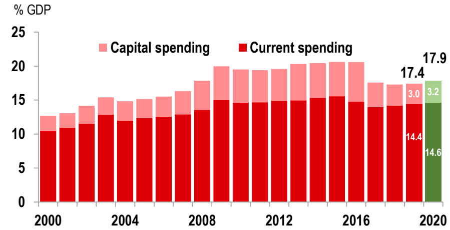
Federal government current account at Banxico
MXNbn*



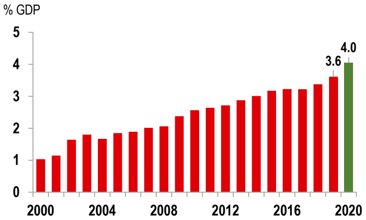
Net budget spending
% GDP



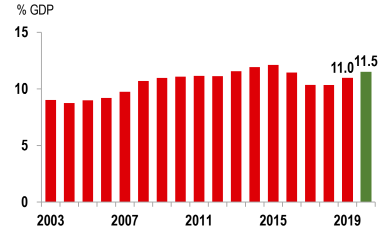
Programmable spending
% GDP



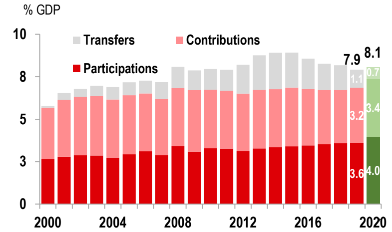
Pensions
% GDP



Social spending
% GDP



Federal spending
% GDP



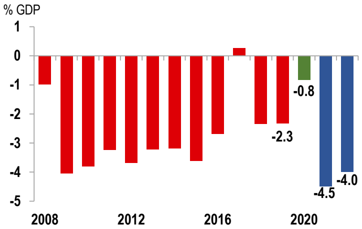
Source: Banorte with data from MoF and INEGI. Data according to availability. *Estimates for 2020 and 2021: General Economic Policy Guidelines 2020 and 2021 preliminary document

Public sector debt

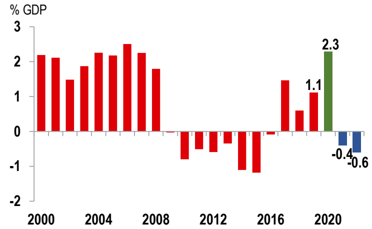
- **Public sector debt has increased in recent years as a result of threefold:**
    1) **Recognized contingent liabilities, particularly derived from Pidiregas (2008);**
    2) **Depreciation of the Mexican peso in the wake of the 2008 crisis; and**
    3) **Realized pension liabilities derived from public pension system reform (2007) and the energy reform of 2013**
- **Meanwhile, financial costs have remained relatively stable between 2% and 3% of GDP**
- **It is worth noting that the composition between internal and external debt has evolved over the years, since the development of the government securities market, so that internal debt now represents 65% of total public sector debt**
- **In this context, the holding of government securities in the hands of foreigners has increased significantly over the years**

Historical series | Year to date | Target in CGPE*

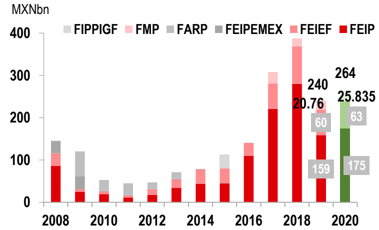
Public deficit (PSBR)
% GDP



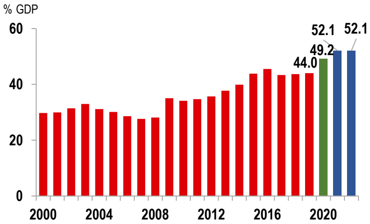
Primary balance
% GDP



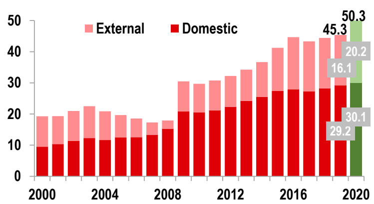
Stabilization funds
MXNbn



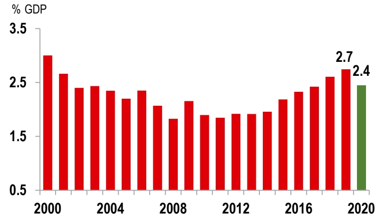
Total Public Sector Debt (HBPSBR)
% GDP



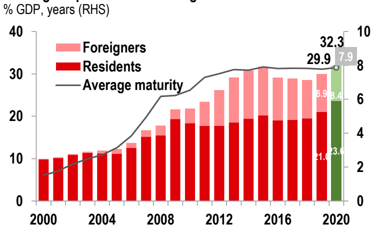
Net Public Sector Debt
% GDP



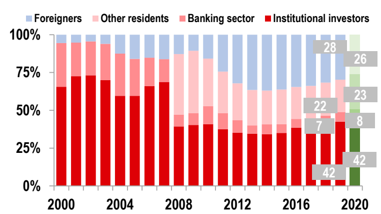
Financial costs
% GDP



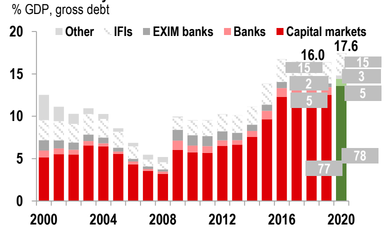
Holdings of peso-denominated government instruments
% GDP, years (RHS)



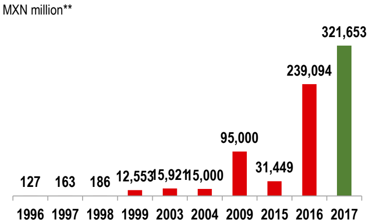
Composition of holdings of government instruments
% total



External debt by source
% GDP, gross debt



Banxico operation surplus
MXN million**



General Economic Policy Guidelines 2021 (Preliminary)

	2020	2021
Gross Domestic Product		
Growth range (% real)	[-3.9 , 0.1]	[1.5 , 3.5]
Nominal (MXNbn)	24,360	25,768
GDP deflator (% y/y)	**3.5**	**3.2**
Inflation (% y/y, end-period)	**3.5**	**3.2**
FX (USD/MXN)		
End-period	22.9	21.4
Average	22.0	21.3
Interest rate (28-day Cetes, %)		
End-period	5.8	5.8
Average	6.2	5.8
Current account		
US$million	-8,928	-16,339
%GDP	-0.8	-1.4
Fiscal balance (%GDP)		
w/capital investments	-3.3	-3.5
ex capital investments	-1.2	-1.5
US variables		
GDP growth (% y/y)	-2.0	2.4
Industrial output (% y/y)	-2.2	2.1
Inflation (% y/y, average)	1.4	1.8
International interest rates		
Libor (3-month)	0.8	0.6
Fed Funds (average)	0.2	0.3
Crude oil (Mexican basket)		
Price (dpb, average)	24.0	30.0
Crude output (mbd)	1,850	2,027
Exports (mbd)	1,075	776
Natural output (average, US$/MTBU)	2.0	2.4

Budget sensitivity 2021

	% GDP
(1) Sensitivity of revenues to 50mbd change in crude oil output	0.04
(2) Sensitivity of revenues to a US$1 change in oil prices	0.05
(3) Sensitivity in tax collection to a 1%-pts change in economic growth	0.06
(4) Sentitivity of financial costs to a 100bps change in interest rates	0.09
(5) Sensitivity from a 20 cent appreciation of the FX	-0.02
Oil revenues	-0.02
Financial costs	0.00
(6) Sensitivity of financial costs to a 100bps change in inflation	0.00

Budget process - Relevant dates

Event	Date
Preliminary budget guidelines	01-Apr
Programatic structure of the budget	30-Jun
Economic guidelines and budget (LIF, PEF & CGPE)	08-Sep
Lower House deadline to approve the Revenue Law	20-Oct
Senate deadline to approve the Revenue Law	31-Oct
Lower House deadline to approve the Spending Budget	15-Nov

Source: Banorte with data from MoF and INEGI. Data according to availability. *Estimates for 2020 and 2021: General Economic Policy Guidelines 2020 and 2021 preliminary document

Making sense of fiscal numbers…

Budget Revenues

- **Public sector revenues (22.2% of GDP in 2019), could be classified in oil revenues (3.9%) and non-oil (18.3%).**

- **In turn, each of these items can be subdivided into revenues from the federal government (16.5% of GDP) and those of other public companies (5.7%), in the case of oil revenues, from Pemex (2.2%).**

- **Federal Government non-oil revenues (14.7% of GDP), include tax collection (13.2%) which comprises, among others, income taxes (ISR: 7%); as well as value added taxes (VAT: 3.9%); along with, excise taxes (IEPS: 1.9%).**

- **Excise taxes are divided in those charged for the sales and imports of alcoholic beverages, beer, sodas, and other beverages as well as of tobacco (non-oil IEPS: 0.7% of GDP), and those charged for the sales and imports of fuel (1.2%).**

- **Fuel excise tax is a fix tax applied to sales and imports of gasoline and fuels. The Federal Government can apply stimulus (i.e. the government decides the percentage of the fix tax that is collected), which could vary weekly, aiming to maintain consumers' purchase parity amid energy prices volatility.**

Net budgetary Expenditures

- **On the spending side, net budgetary expenditures 23.9% of GDP) -gross spending minus amortization, debt from previous fiscal exercises (ADEFAS) and other amounts of approved spending not exercised-, could be classified as programmable (17.5%) -spending directed to government operations-, and non-programmable (6.4%), used for the fulfillment of obligations and other spending determined by Law, such as public debt, transfers to states and municipalities, among others, which implies that it is not aimed to finance Federal Government current operations.**

- **A particular item within programmable spending is the amount destined to pensions (3.6% of GDP in 2019), which has been trending upward for some years now.**

- **Public spending could also be classified according to the purpose it serves. Within this dimension, social spending (11%), is destined to finance the government's social development goals (health, education, etc.).**

- **Federalized spending (7.9% of GDP) are the resources transfered by the Federal Government to states and municipalities through: participations (3.6%), contributions (3.2%), and other transfers (1.1%).**

Public sector balance

- **The difference between budgetary revenues (22.2% of GDP) and net budgetary spending (23.9% of GDP) is knowns as the traditional public balance (-1.7% of GDP).**

- **Primary balance represents 1.1% of GDP and it is defined as budget revenues (22.2%) minus net budget spending (23.9%), excluding financial costs (2.7%).**

- **When financial requirements from Pidiregas (contingent liabilities from certain infrastructure projects), IPAB (*Instituto para la Protección del Ahorro Bancario*), other debt programs, development banks, etc, are added, we obtain a wider definition of the balance of the public sector known as *Public Sector Borrowing Requirements* (PSBR: -2.3%).**

Net public sector debt

- **Net public sector debt are the public sector commitments (45.3% of GDP in 2019), net of financial assets, such as stabilization funds.**

- **According to the currency in which the instruments are denominated, debt is classified as domestic (29.2% of GDP), when the debt is denominated in local currency and paid to residents; or external (16.1% of GDP) in the case of debt denominated in a currency different to the Mexican peso to non-residents.**

- **The most comprehensive measure of public sector debt is the *Historical Balance of Public Sector Government Requirements* (HBPSBR): 44% of GDP in 2019, which includes public sector net debt, along with net financial requirements from IPAB, Pidiregas, other government debt programs, etc.**

Stabilization Funds

FEIP - Budgetary revenues stabilization fund (*Fondo de Estabilización de Ingresos Presupuestales*)

FEIEF - Federal States Governments' revenues stabilization fund (*Fondo de Estabilización de Ingresos de Entidades Federativas*)

FMP - Mexican Crude Oil Fund (*Fondo Mexicano del Petróleo*)

FEIPEMEX - Pemex revenues stabilization funds (*Fondo de Estabilización de Ingresos de Pemex*)

FARP - Pension restructuring support fund (*Fondo de Apoyo para la Reestructura de Pensiones*)

FIPPIGF - Federal Government progams and infrastructure projects stabilization fund (*Fondo de Inversiones para Programas y Proyectos de Infraestrutura del Gobierno Federal*)

Certification of Analysts.

We, Gabriel Casillas Olvera, Alejandro Padilla Santana, Delia María Paredes Mier, Juan Carlos Alderete Macal, Manuel Jiménez Zaldívar, Marissa Garza Ostos, Tania Abdul Massih Jacobo, Francisco José Flores Serrano, Katia Celina Goya Ostos, Santiago Leal Singer, José Itzamna Espitia Hernández, Valentín III Mendoza Balderas, Víctor Hugo Cortes Castro, Hugo Armando Gómez Solís, Miguel Alejandro Calvo Domínguez, Luis Leopoldo López Salinas, Leslie Thalía Orozco Vélez, Gerardo Daniel Valle Trujillo and Eridani Ruibal Ortega, certify that the points of view expressed in this document are a faithful reflection of our personal opinion on the company (s) or firm (s) within this report, along with its affiliates and/or securities issued. Moreover, we also state that we have not received, nor receive, or will receive compensation other than that of Grupo Financiero Banorte S.A.B. of C.V for the provision of our services.

Relevant statements.

In accordance with current laws and internal procedures manuals, analysts are allowed to hold long or short positions in shares or securities issued by companies that are listed on the Mexican Stock Exchange and may be the subject of this report; nonetheless, equity analysts have to adhere to certain rules that regulate their participation in the market in order to prevent, among other things, the use of private information for their benefit and to avoid conflicts of interest. Analysts shall refrain from investing and holding transactions with securities or derivative instruments directly or through an intermediary person, with Securities subject to research reports, from 30 calendar days prior to the issuance date of the report in question, and up to 10 calendar days after its distribution date.

Compensation of Analysts.

Analysts' compensation is based on activities and services that are aimed at benefiting the investment clients of Casa de Bolsa Banorte and its subsidiaries. Such compensation is determined based on the general profitability of the Brokerage House and the Financial Group and on the individual performance of each analyst. However, investors should note that analysts do not receive direct payment or compensation for any specific transaction in investment banking or in other business areas.

Last-twelve-month activities of the business areas.

Grupo Financiero Banorte S.A.B. de C.V., *through its business areas, provides services that include, among others, those corresponding to investment banking and corporate banking, to a large number of companies in Mexico and abroad. It may have provided, is providing or, in the future, will provide a service such as those mentioned to the companies or firms that are the subject of this report. Casa de Bolsa Banorte or its affiliates receive compensation from such corporations in consideration of the aforementioned services.*

Over the course of the last twelve months, Grupo Financiero Banorte S.A.B. C.V., has not obtained compensation for services rendered by the investment bank or by any of its other business areas of the following companies or their subsidiaries, some of which could be analyzed within this report.

Activities of the business areas during the next three months.

Casa de Bolsa Banorte, Grupo Financiero Banorte or its subsidiaries expect to receive or intend to obtain revenue from the services provided by investment banking or any other of its business areas, by issuers or their subsidiaries, some of which could be analyzed in this report.

Securities holdings and other disclosures.

As of the end of last quarter, Grupo Financiero Banorte S.A.B. of C.V. has not held investments, directly or indirectly, in securities or derivative financial instruments, whose underlying securities are the subject of recommendations, representing 1% or more of its investment portfolio of outstanding securities or 1 % of the issuance or underlying of the securities issued.

None of the members of the Board of Grupo Financiero Banorte and Casa de Bolsa Banorte, along general managers and executives of an immediately below level, have any charges in the issuers that may be analyzed in this document.

The Analysts of Grupo Financiero Banorte S.A.B. of C.V. do not maintain direct investments or through an intermediary person, in the securities or derivative instruments object of this analysis report.

Guide for investment recommendations.

	Reference
BUY	*When the share expected performance is greater than the MEXBOL estimated performance.*
HOLD	*When the share expected performance is similar to the MEXBOL estimated performance.*
SELL	*When the share expected performance is lower than the MEXBOL estimated performance.*

Even though this document offers a general criterion of investment, we urge readers to seek advice from their own Consultants or Financial Advisors, in order to consider whether any of the values mentioned in this report are in line with their investment goals, risk and financial position.

Determination of Target Prices

For the calculation of estimated target prices for securities, analysts use a combination of methodologies generally accepted among financial analysts, including, but not limited to, multiples analysis, discounted cash flows, sum-of-the-parts or any other method that could be applicable in each specific case according to the current regulation. No guarantee can be given that the target prices calculated for the securities will be achieved by the analysts of Grupo Financiero Banorte S.A.B. C.V, since this depends on a large number of various endogenous and exogenous factors that affect the performance of the issuing company, the environment in which it performs, along with the influence of trends of the stock market, in which it is listed. Moreover, the investor must consider that the price of the securities or instruments can fluctuate against their interest and cause the partial and even total loss of the invested capital.

GRUPO FINANCIERO BANORTE S.A.B. de C.V.

Research and Strategy			
Gabriel Casillas Olvera	IRO and Chief Economist	gabriel.casillas@banorte.com	(55) 4433 - 4695
Raquel Vázquez Godinez	Assistant	raquel.vazquez@banorte.com	(55) 1670 - 2967
Lourdes Calvo Fernández	Analyst (Edition)	lourdes.calvo@banorte.com	(55) 1103 - 4000 x 2611
Economic Research and Financial Market Strategy			
Alejandro Padilla Santana	Executive Director of Economic Research and Financial Markets Strategy	alejandro.padilla@banorte.com	(55) 1103 - 4043
Itzel Martínez Rojas	Analyst	itzel.martinez.rojas@banorte.com	(55) 1670 - 2251
Economic Research			
Juan Carlos Alderete Macal, CFA	Director of Economic Research	juan.alderete.macal@banorte.com	(55) 1103 - 4046
Francisco José Flores Serrano	Senior Economist, Mexico	francisco.flores.serrano@banorte.com	(55) 1670 - 2957
Katia Celina Goya Ostos	Senior Economist, Global	katia.goya@banorte.com	(55) 1670 - 1821
Luis Leopoldo López Salinas	Economist, Global	luis.lopez.salinas@banorte.com	(55) 1103 - 4000 x 2707
Market Strategy			
Manuel Jiménez Zaldívar	Director of Market Strategy	manuel.jimenez@banorte.com	(55) 5268 - 1671
Fixed income and FX Strategy			
Santiago Leal Singer	Senior Strategist, Fixed Income and FX	santiago.leal@banorte.com	(55) 1670 - 2144
Leslie Thalía Orozco Vélez	Strategist, Fixed Income and FX	leslie.orozco.velez@banorte.com	(55) 5268 - 1698
Equity Strategy			
Marissa Garza Ostos	Director of Equity Strategy	marissa.garza@banorte.com	(55) 1670 - 1719
José Itzamna Espitia Hernández	Senior Strategist, Equity	jose.espitia@banorte.com	(55) 1670 - 2249
Valentín III Mendoza Balderas	Senior Strategist, Equity	valentin.mendoza@banorte.com	(55) 1670 - 2250
Víctor Hugo Cortes Castro	Senior Strategist, Technical	victorh.cortes@banorte.com	(55) 1670 - 1800
Eridani Ruibal Ortega	Analyst	eridani.ruibal.ortega@banorte.com	(55) 1103 - 4000 x 2755
Corporate Debt			
Tania Abdul Massih Jacobo	Director of Corporate Debt	tania.abdul@banorte.com	(55) 5268 - 1672
Hugo Armando Gómez Solís	Senior Analyst, Corporate Debt	hugoa.gomez@banorte.com	(55) 1670 - 2247
Gerardo Daniel Valle Trujillo	Analyst, Corporate Debt	gerardo.valle.trujillo@banorte.com	(55) 1670 - 2248
Economic Studies			
Delia María Paredes Mier	Executive Director of Economic Studies	delia.paredes@banorte.com	(55) 5268 - 1694
Miguel Alejandro Calvo Domínguez	Senior Analyst, Economic Studies	miguel.calvo@banorte.com	(55) 1670 - 2220
Wholesale Banking			
Armando Rodal Espinosa	Head of Wholesale Banking	armando.rodal@banorte.com	(81) 8319 - 6895
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.ceballos@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 Corporate Banking	pimentelr@banorte.com	(55) 5268 - 9004
Ricardo Velázquez Rodríguez	Head of International Banking	rvelazquez@banorte.com	(55) 5004 - 5279
Víctor Antonio Roldan Ferrer	Head of Commercial Banking	victor.roldan.ferrer@banorte.com	(55) 5004 - 1454