

MEXICO: ECONOMIC OUTLOOK

AS/COA MONTERREY 2016

INVESTMENT OPPORTUNITIES AND URBAN INNOVATION IN NUEVO LEÓN

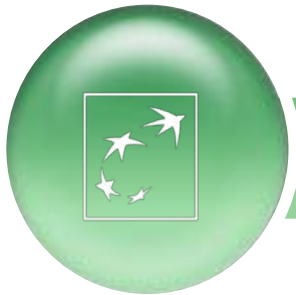
SEPTEMBER 2016

LATIN AMERICA MARKET ECONOMICS
MARCELO CARVALHO



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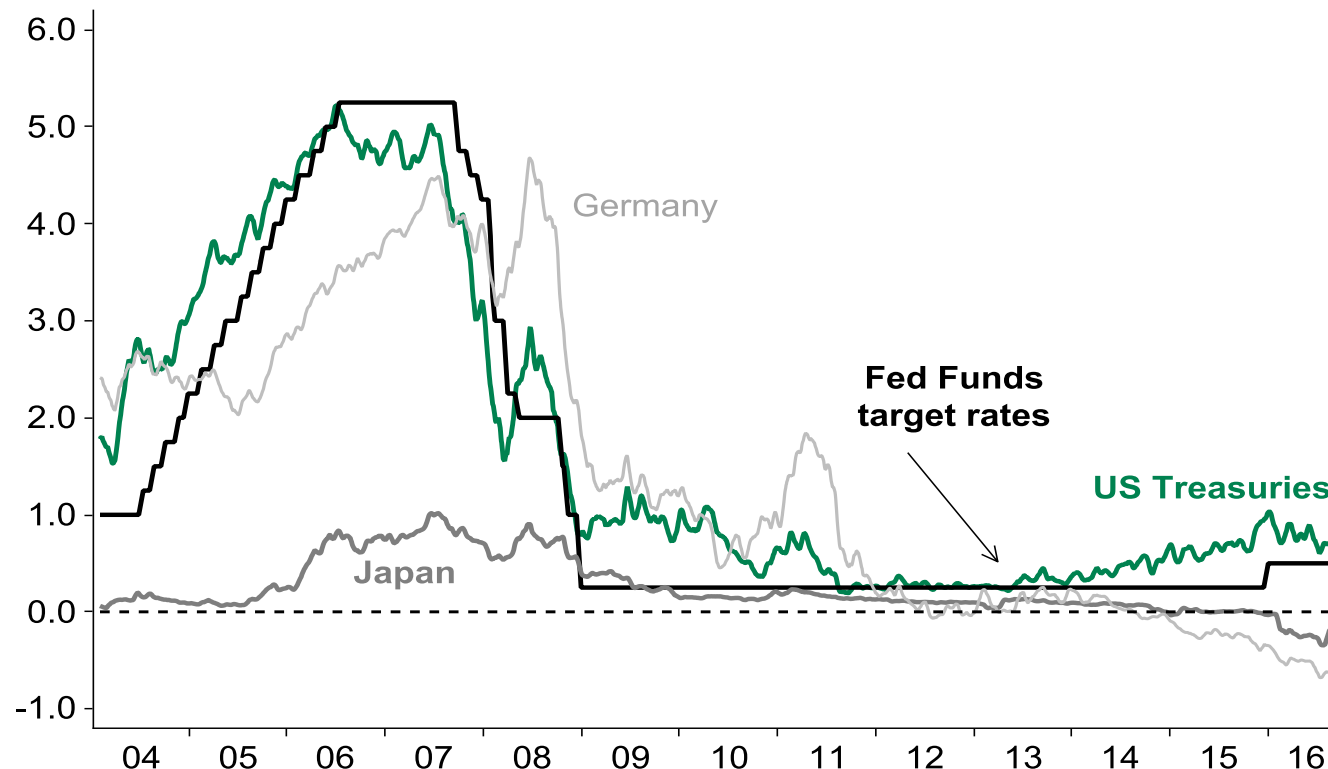


Mexico in the global context



US: GLOBAL MONETARY POLICY IS CHANGING

Fed Funds target rate and 2-year treasury bond yields (% a.r.)



Source: ECB, FED, BoJ, Macrobond, BNP Paribas



Global monetary policy divergence: rates are up in US, but down in Eurozone and Japan

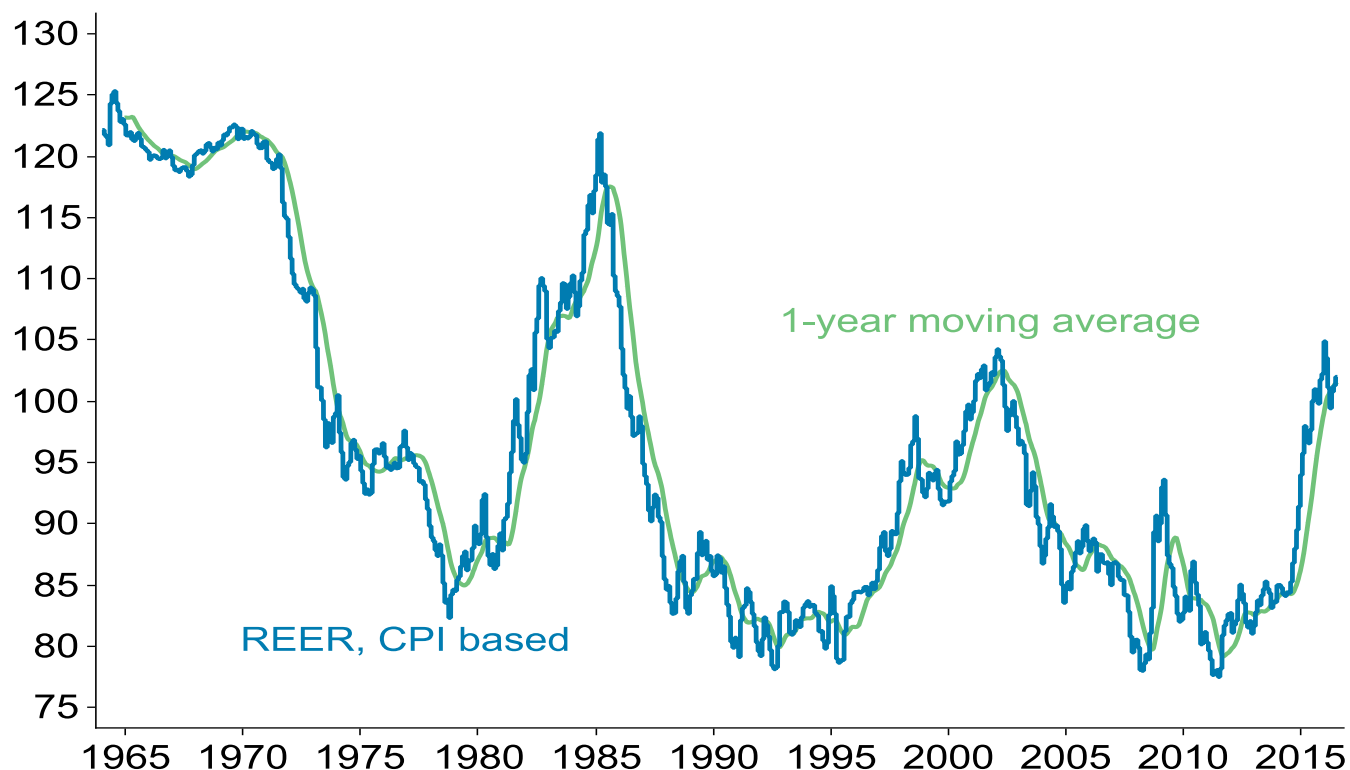


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GLOBAL: US DOLLAR CYCLES IN HISTORICAL PERSPECTIVE

US Real effective exchange rate index (1973=100)



Source: FED, Macrobond, BNP Paribas.



USD appreciation comes in waves

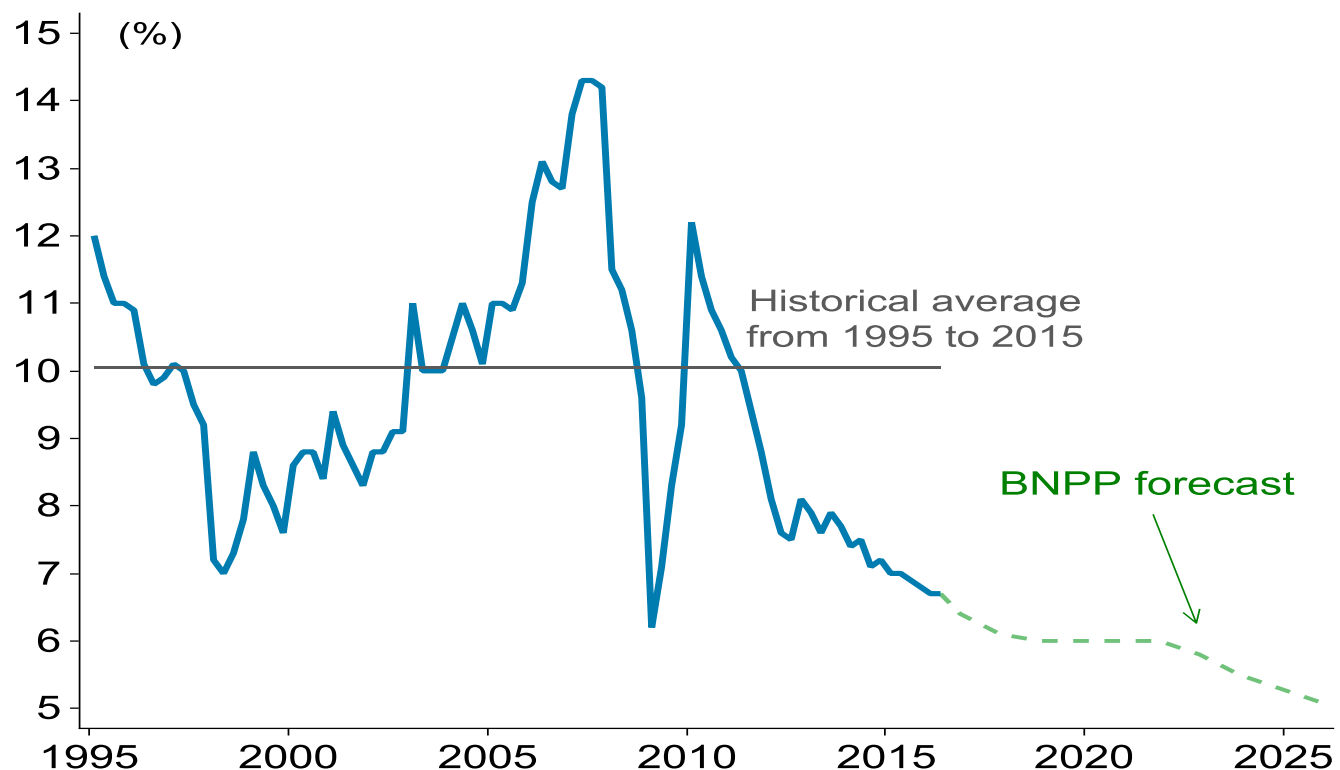


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CHINA: SLOWER GROWTH AHEAD

China annual real GDP growth (%)



Source: NBS, Macrobond, BNP Paribas. Dotted lines show BNP forecasts.



Chinese growth is set to be slower in the next decade than it was in the last decade

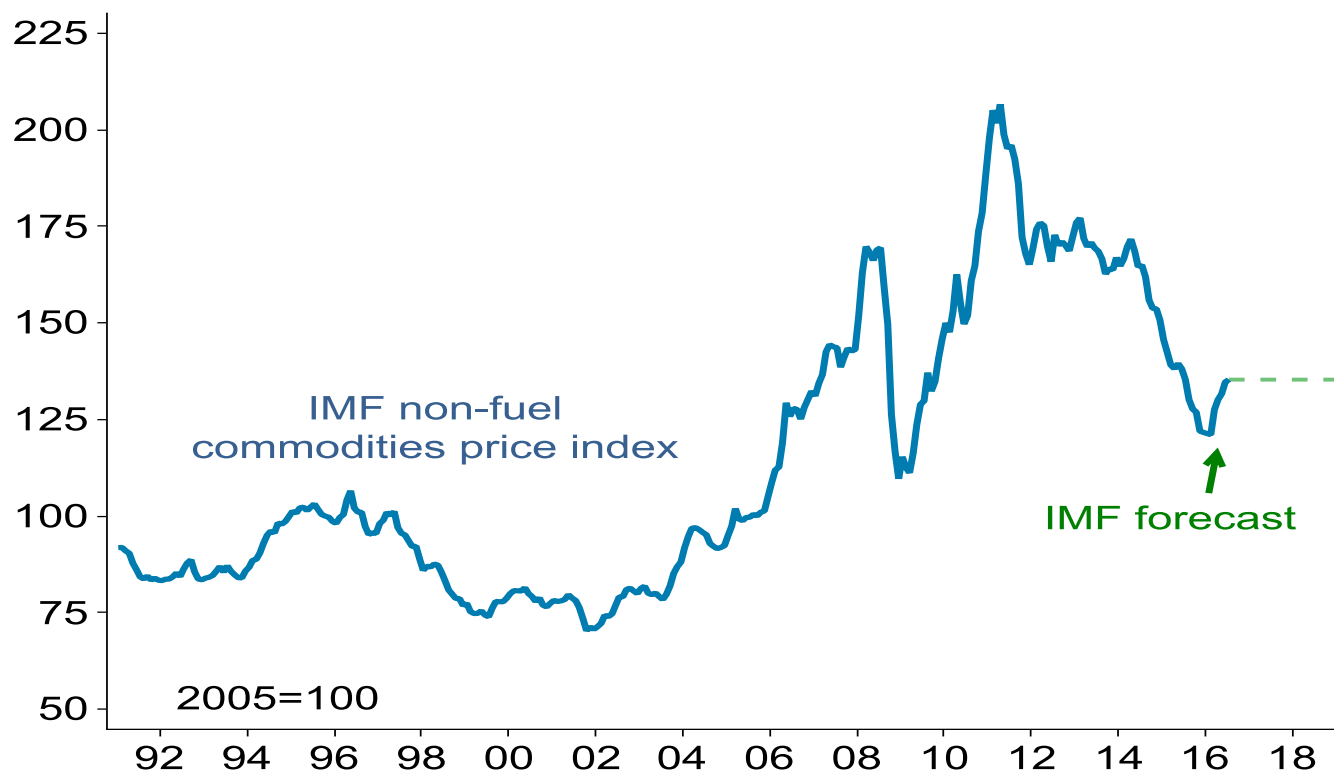


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GLOBAL: COMMODITY PRICE BOOM IS OVER

IMF non-fuel commodities price index (2005=100)



Source: IMF, Macrobond, BNP Paribas. Dotted lines show IMF forecasts.



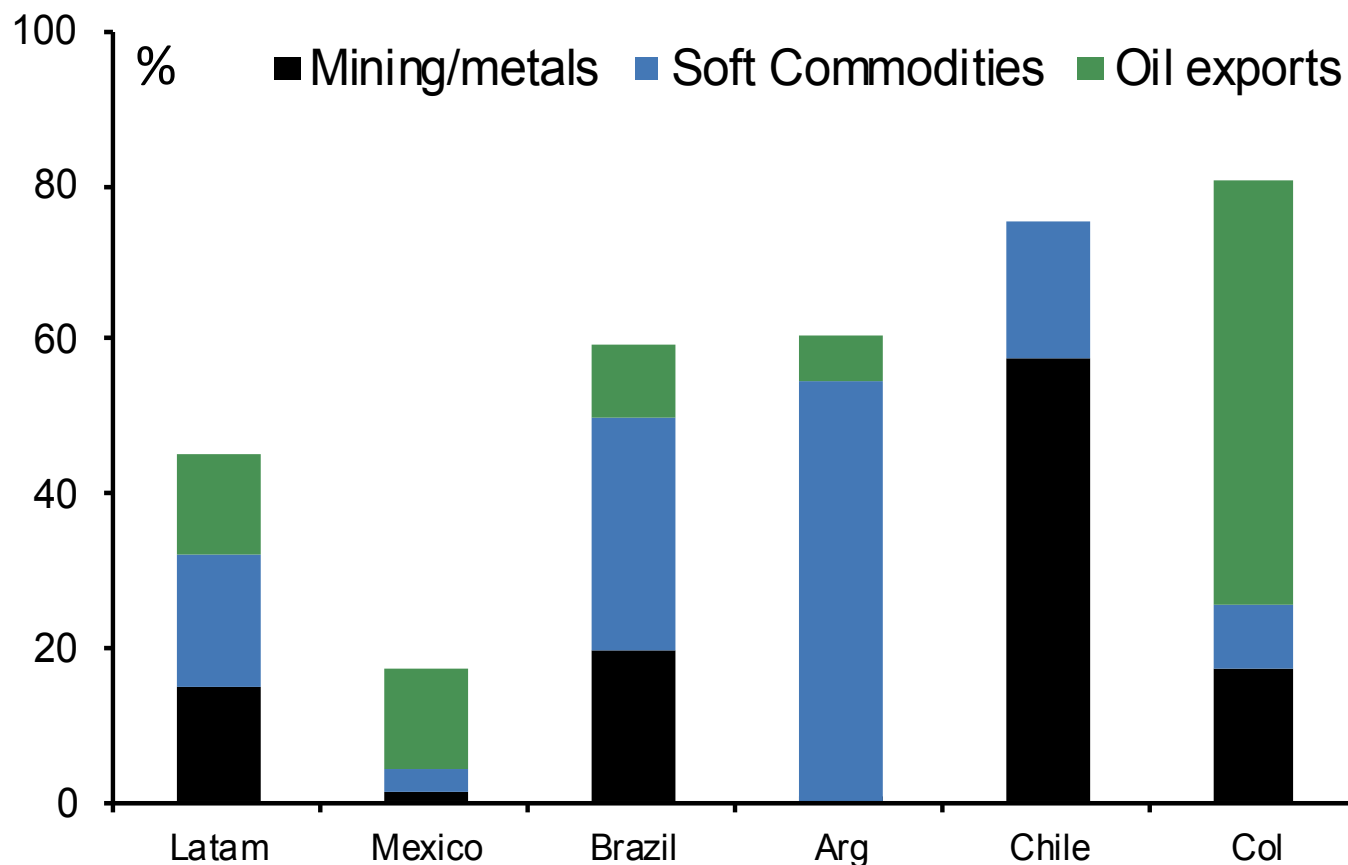
We should not count on another commodity price supercycle soon



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LATAM: COMMODITIES AS A SHARE OF LATAM EXPORTS (%)



Source: National statistics offices, BNP Paribas; Ratios based on 2013 data



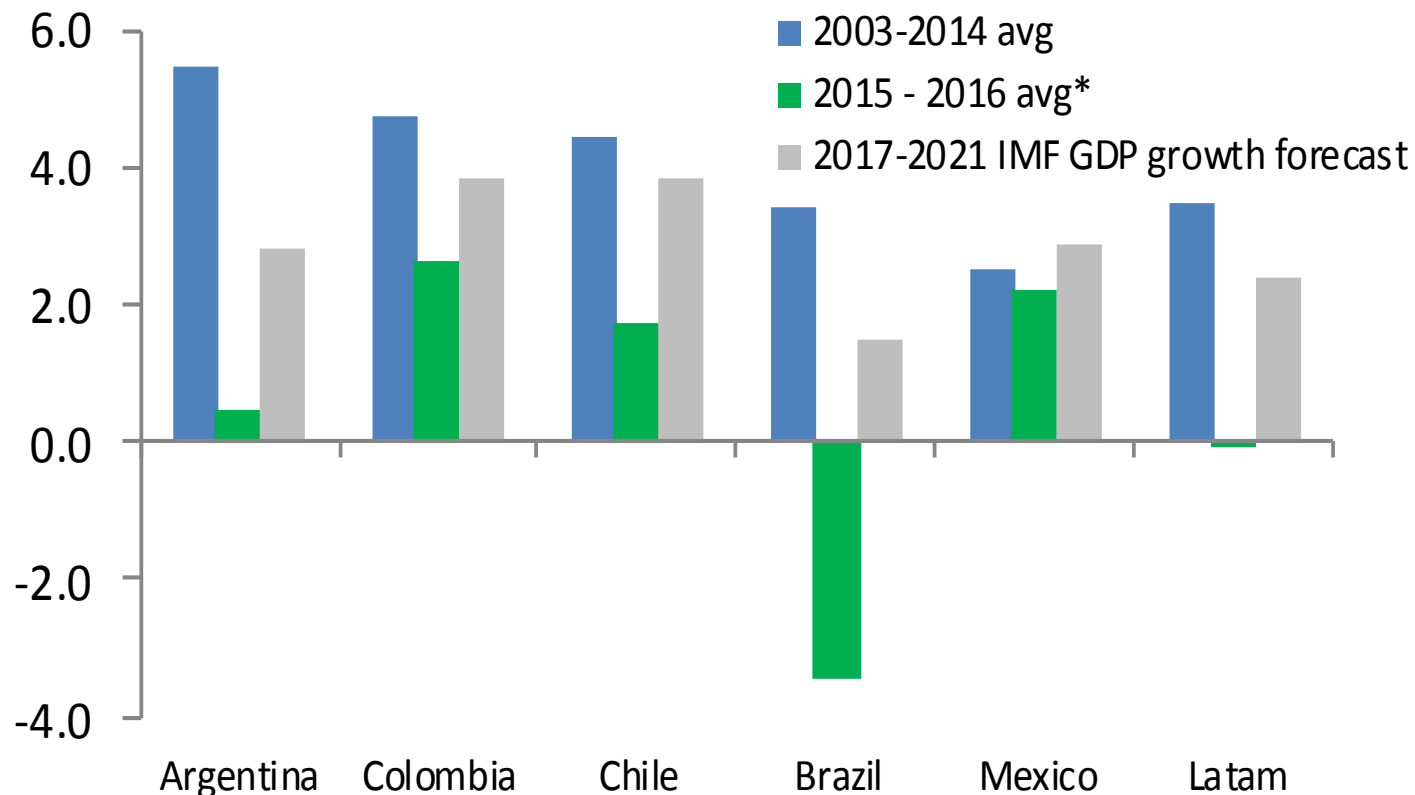
Export exposure to commodities varies across the region



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LATAM: REAL GDP GROWTH PERFORMANCE (% y/y)



Source: IMF, BNP Paribas; *BNPP forecasts



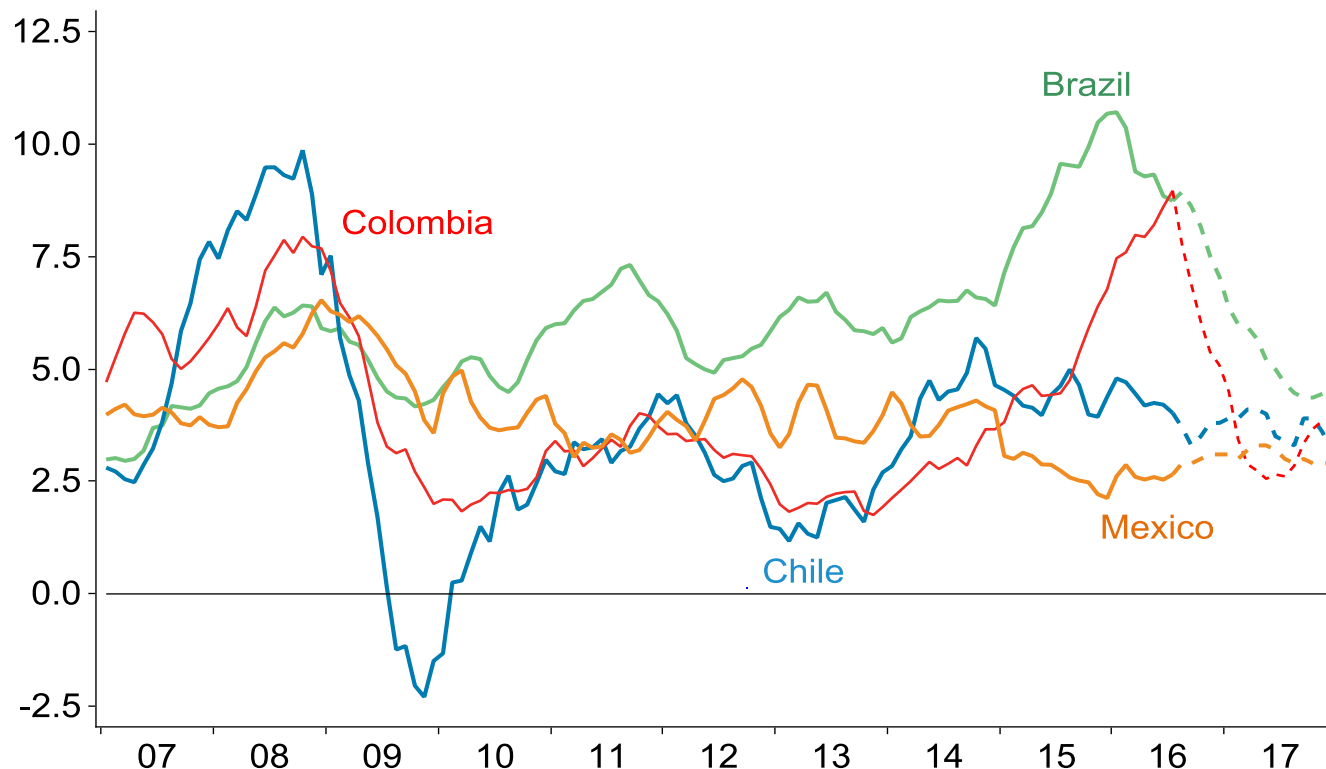
Growth is down from the golden days of the commodity price boom, but should recover



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LATAM: CPI INFLATION (% y/y)



Source: IBGE, INE, DANE, INEGI, INEI, Macrobond, BNP Paribas. Dotted lines are BNPP forecasts



Back toward targets

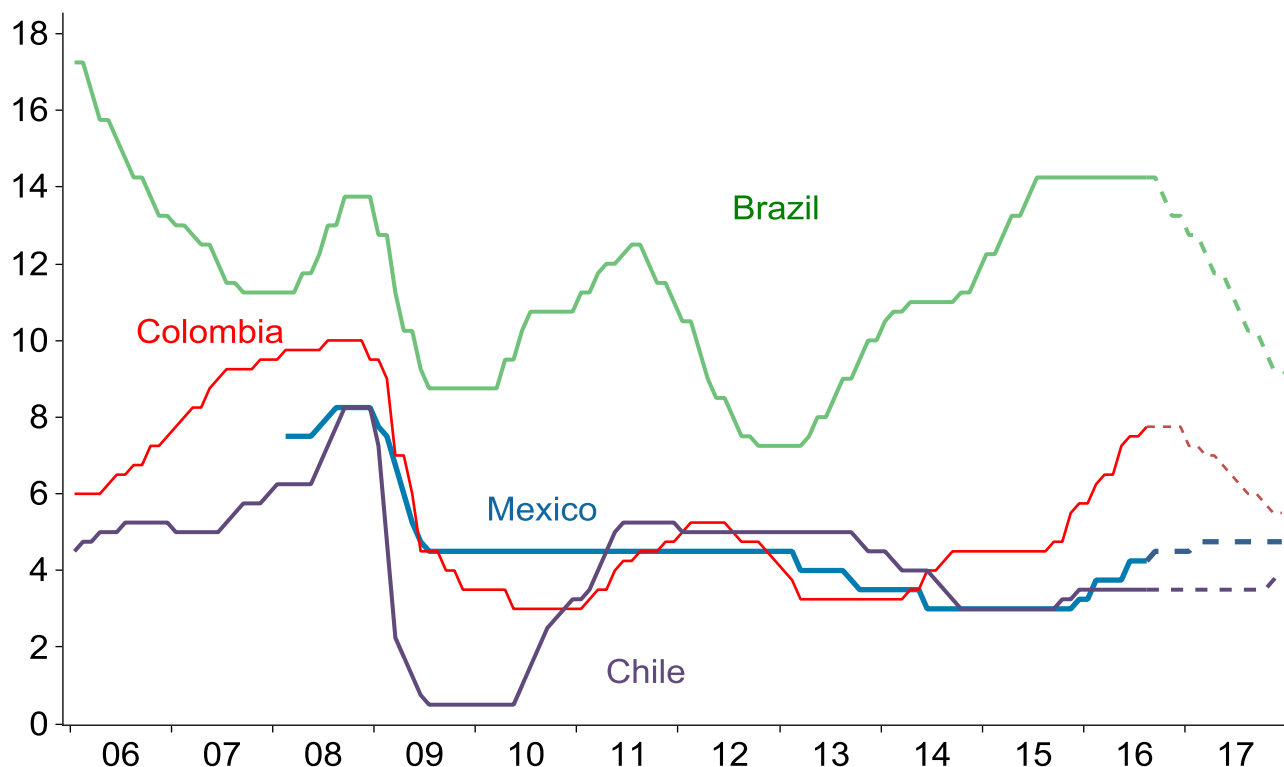


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LATAM: POLICY INTEREST RATES

Latam: Policy rate cycles (% per annum)



Source: BCB, BM, BCC, BR, BCRP, Macrobond, BNP Paribas. Dotted lines are BNPP forecasts



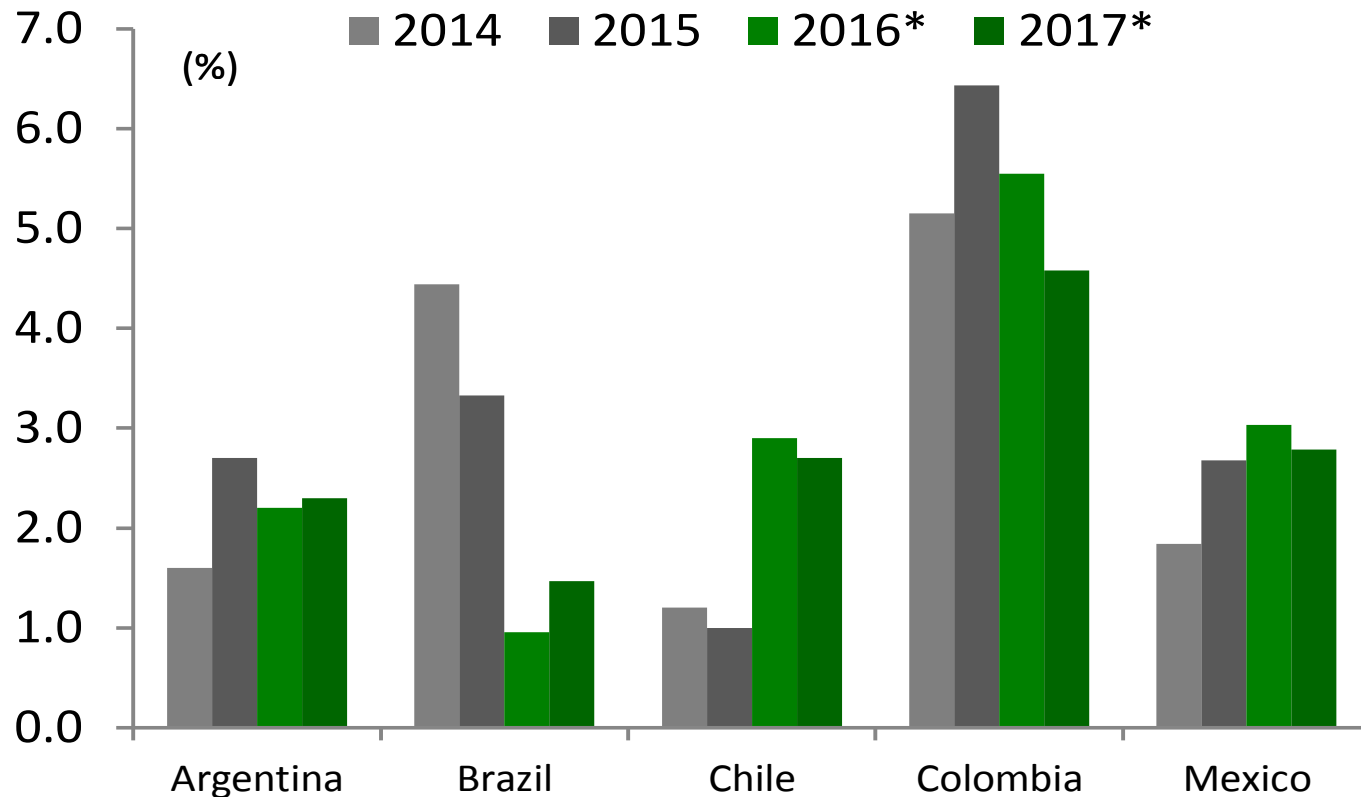
Shifting monetary policy paths



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LATAM: CURRENT ACCOUNT DEFICITS (% OF GDP)



Source: IMF, BNP Paribas. * represent BNPP forecasts



Latam faces significant current account deficits

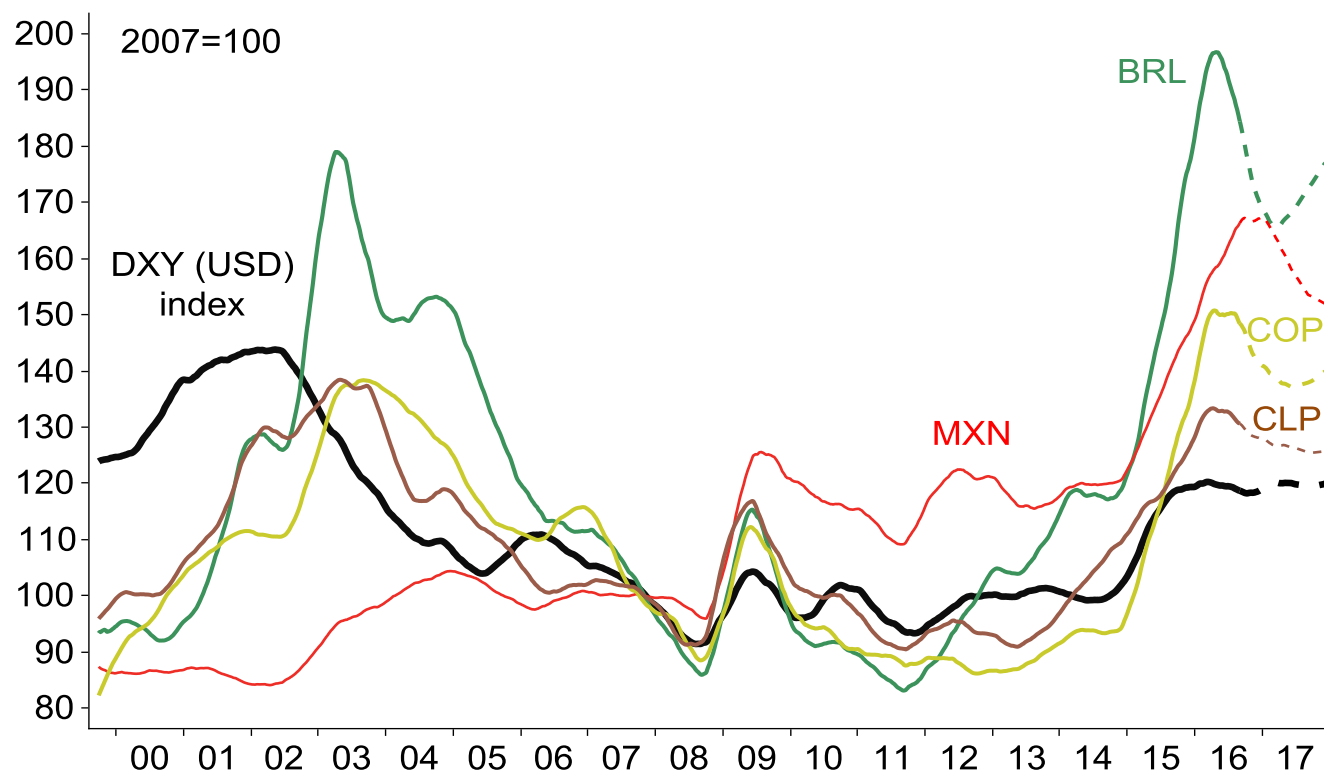


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LATAM: EXCHANGE RATES AGAINST THE USD

(UP MEANS A STRONGER DOLLAR)



Source: Macrobond, BNP Paribas; 180-day moving average



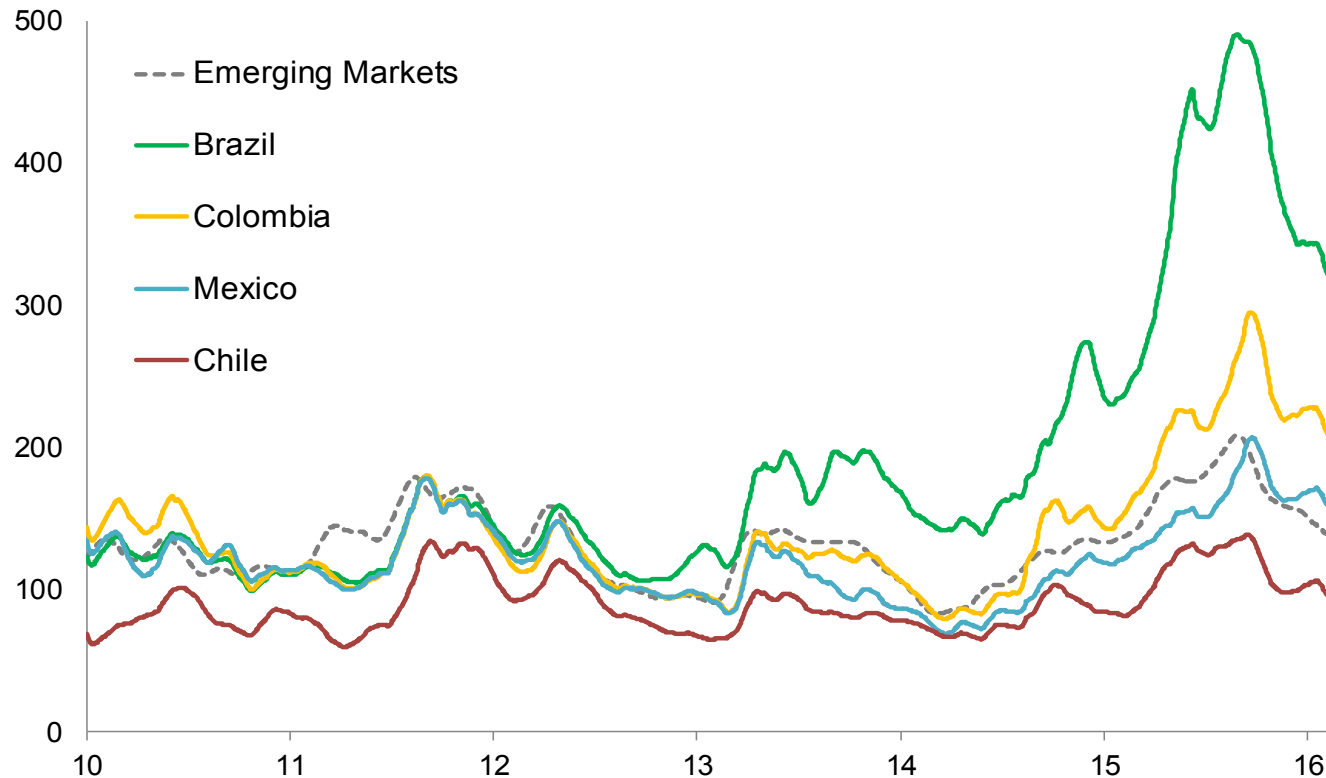
Stronger USD means weaker Latam currencies



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LATAM: CREDIT DEFAULT SWAPS (5-YEAR SPREADS, BPS)



Source: Bloomberg, BNP Paribas; 30-day moving average



CDS spreads reflect market perceptions about country risk premium



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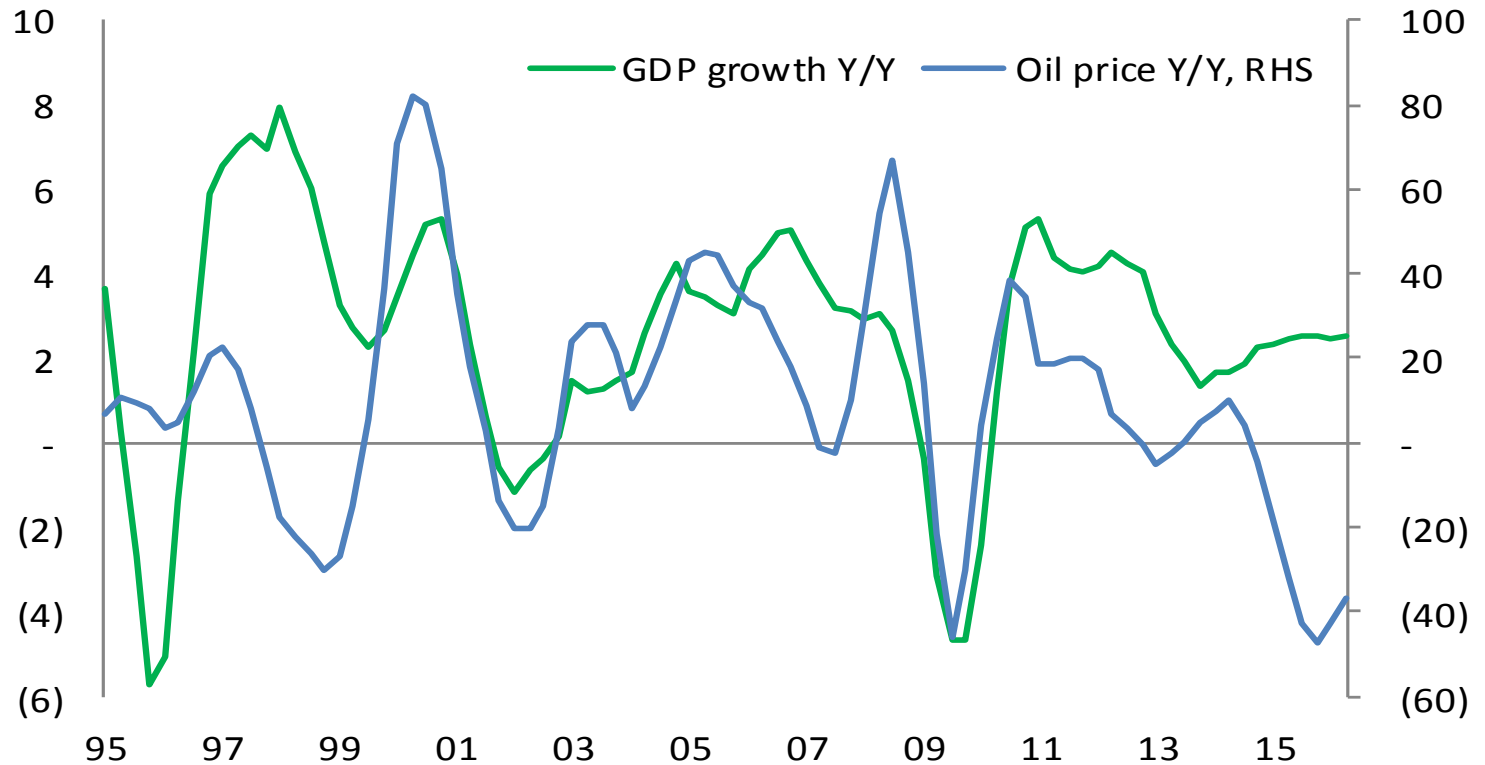
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Mexico: Oil is not well



MEXICO: REAL GDP GROWTH AND OIL PRICES, % Y/Y



Source: Bloomberg, INEGI, BNP Paribas



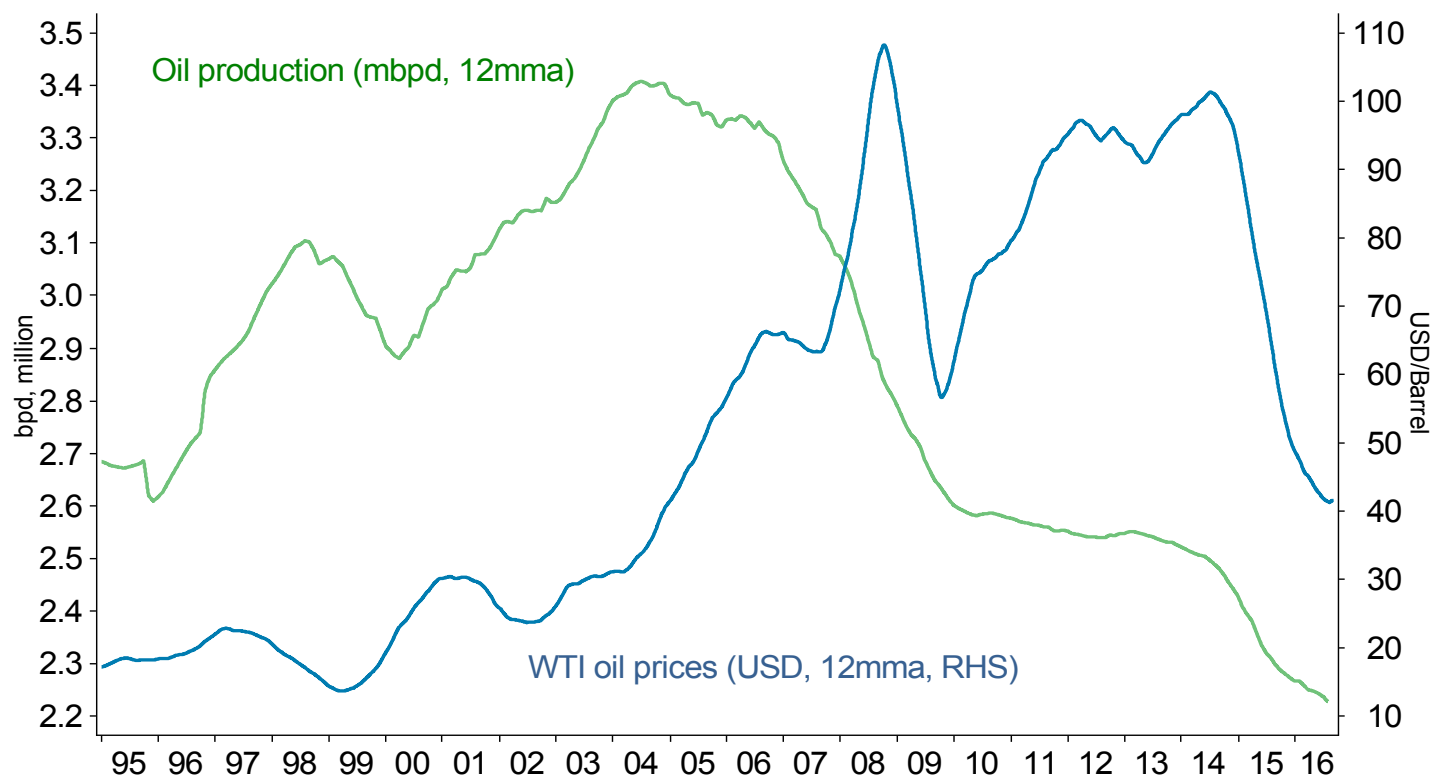
The correlation between real GDP growth and international oil prices is significant



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MEXICO: OIL PRODUCTION AND PRICES



Source: Bloomberg, PEMEX, BNP Paribas



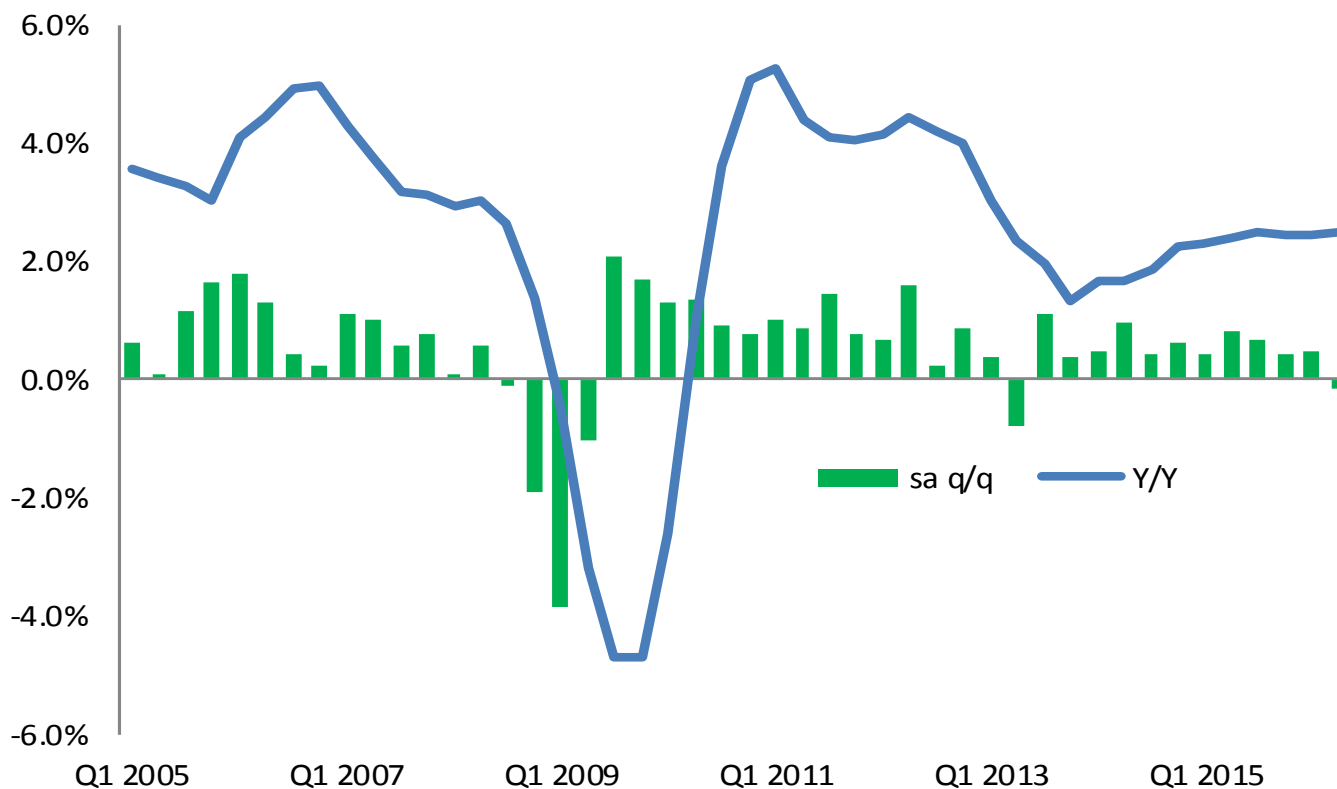
Mexico's oil problem is not just prices



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MEXICO: GDP GROWTH (%)



Source: Macrobond, Inegi, BNP Paribas



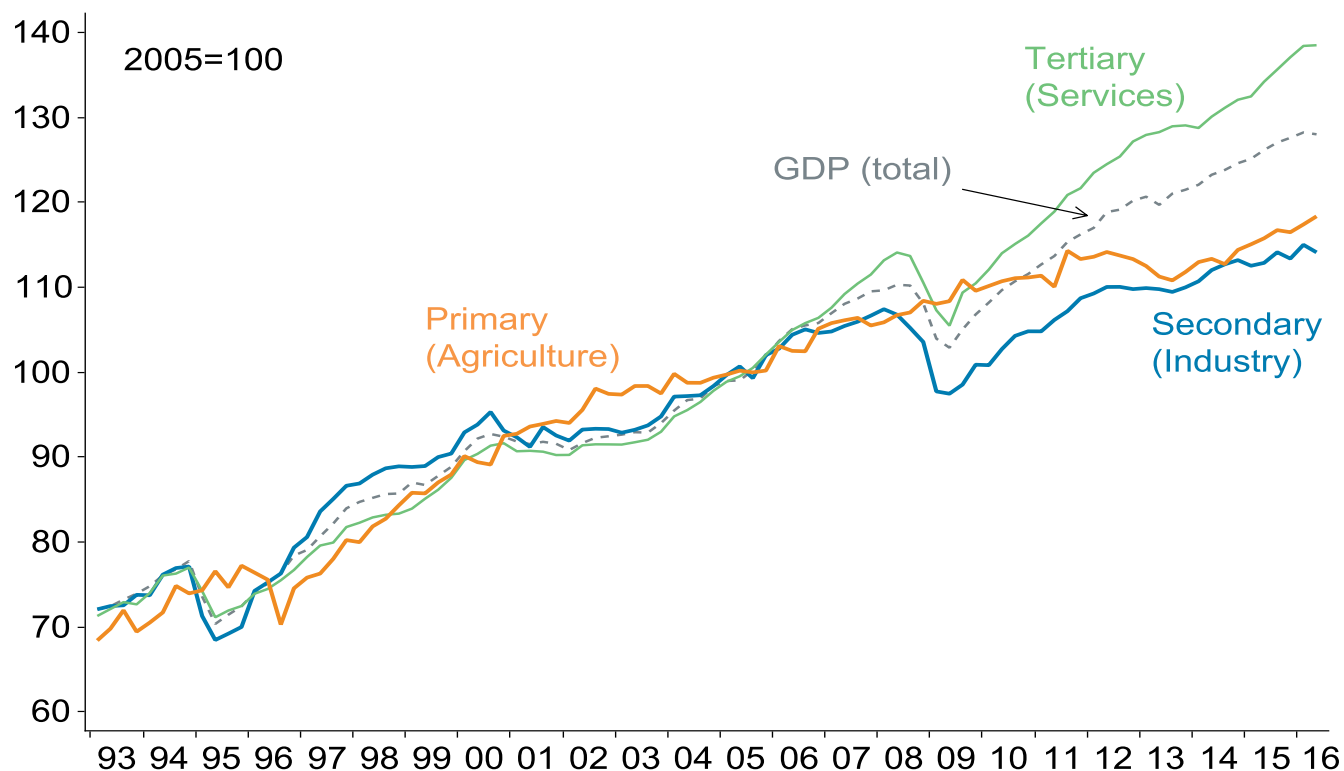
Real GDP growth was down in Q2, while prospects look challenging



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MEXICO: GDP COMPONENTS (SUPPLY SIDE)



Source: Inegi, Macrobond, BNP Paribas



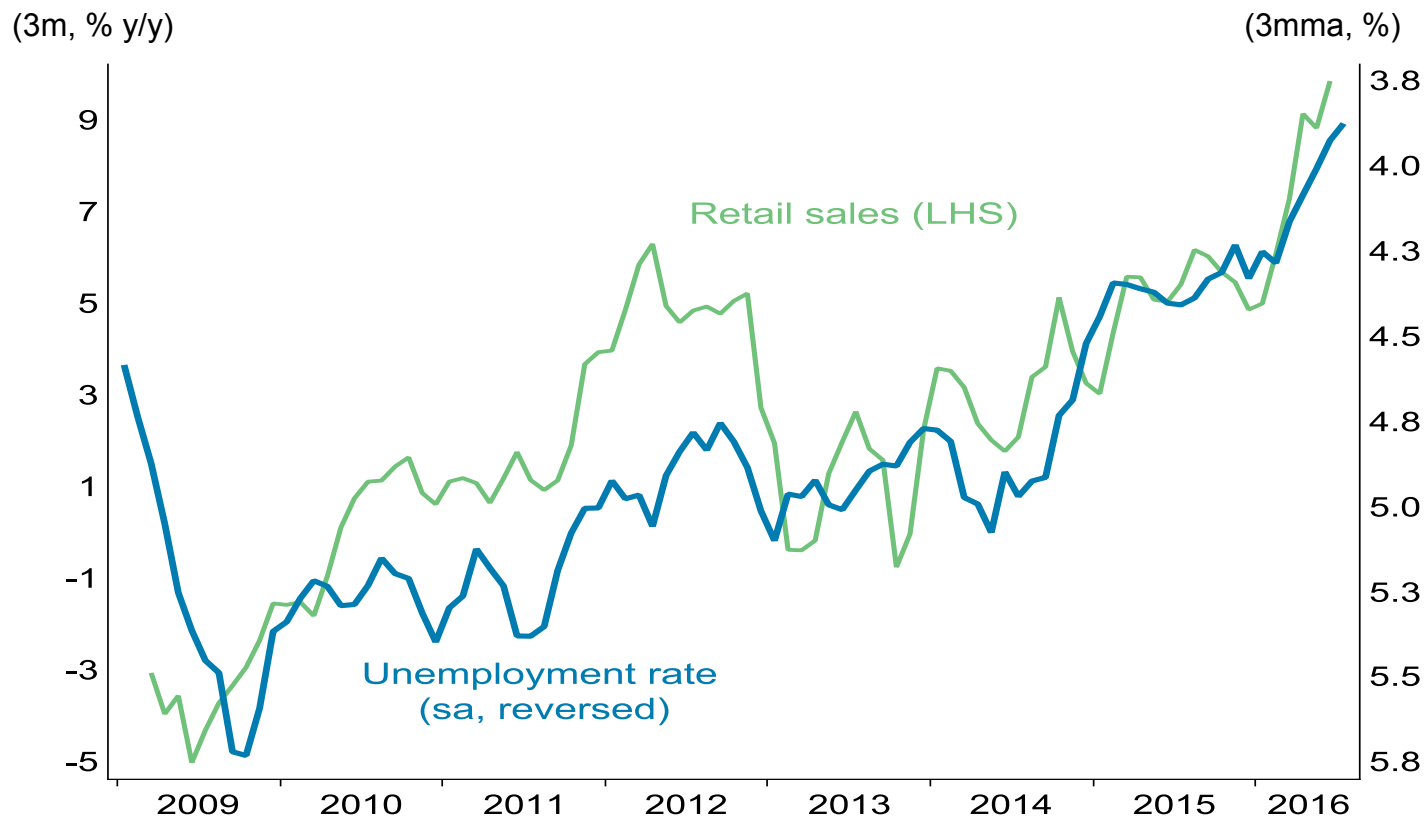
Growth dichotomy: Services outperform, while industry lags behind



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MEXICO: PRIVATE CONSUMPTION CONTINUES TO STRENGTHEN



Source: Macrobond, Inegi, BNP Paribas



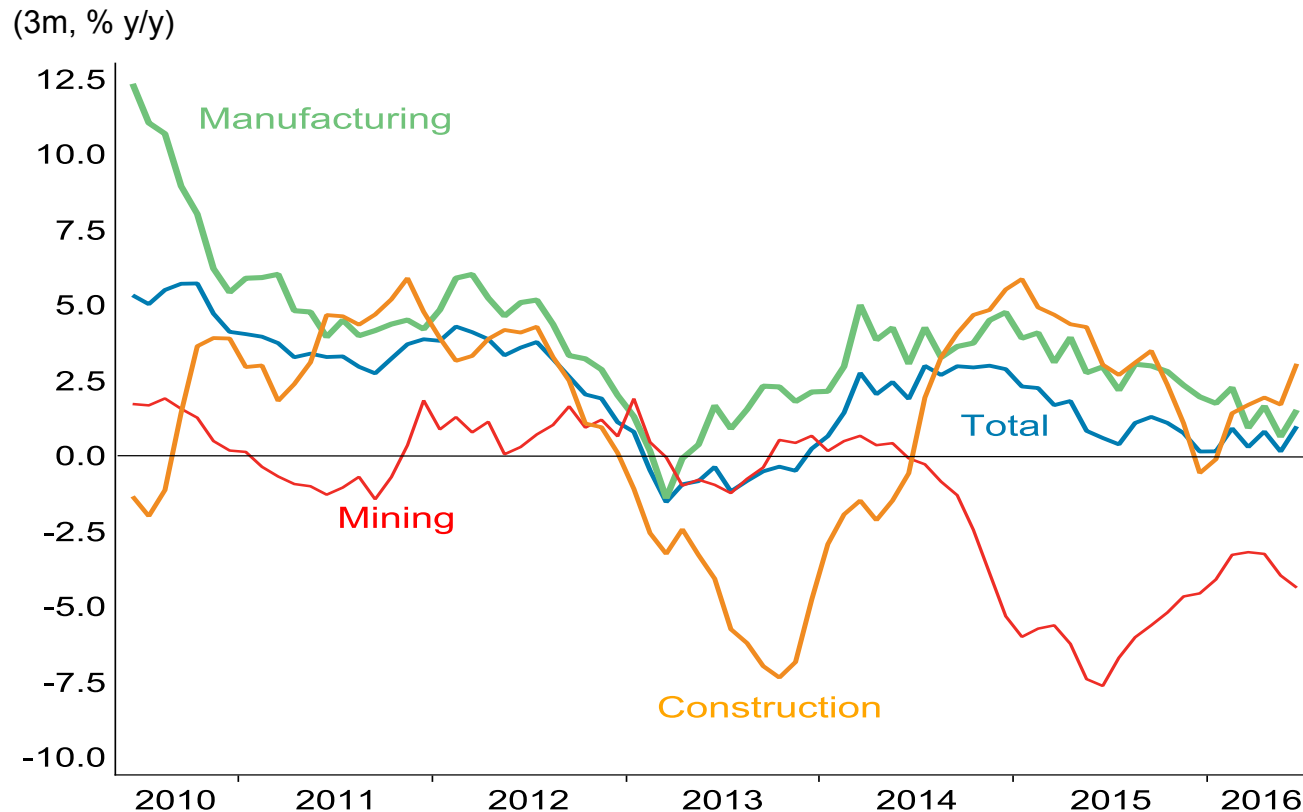
Stronger labor market and rising real incomes boost consumer spending



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MEXICO: INDUSTRIAL PRODUCTION GROWTH AND ITS COMPONENTS



Source: Macrobond, Inegi, BNP Paribas



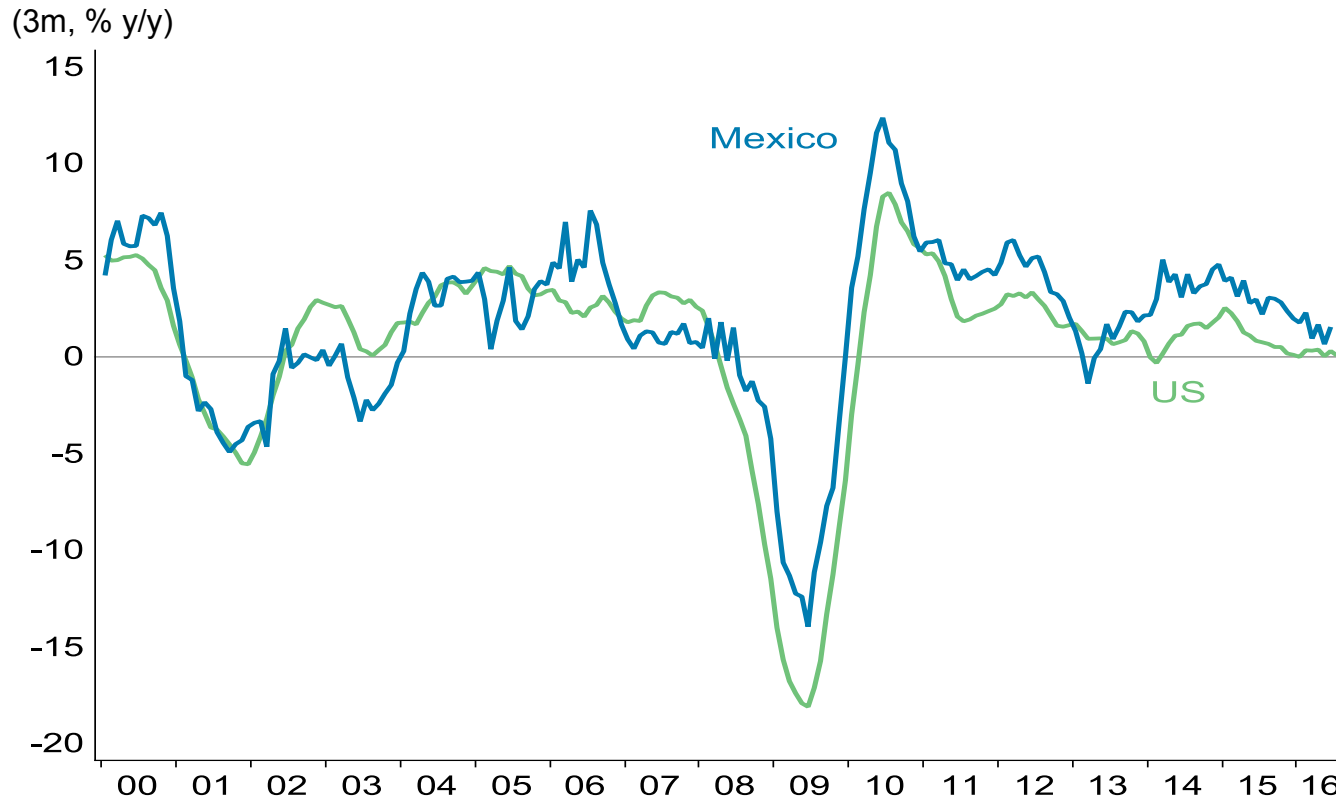
Soft external demand likely to keep manufacturing activity subdued for now



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MEXICO AND US: MANUFACTURING SECTOR GROWTH



Source: Inegi, Federal Reserve, BNP Paribas.



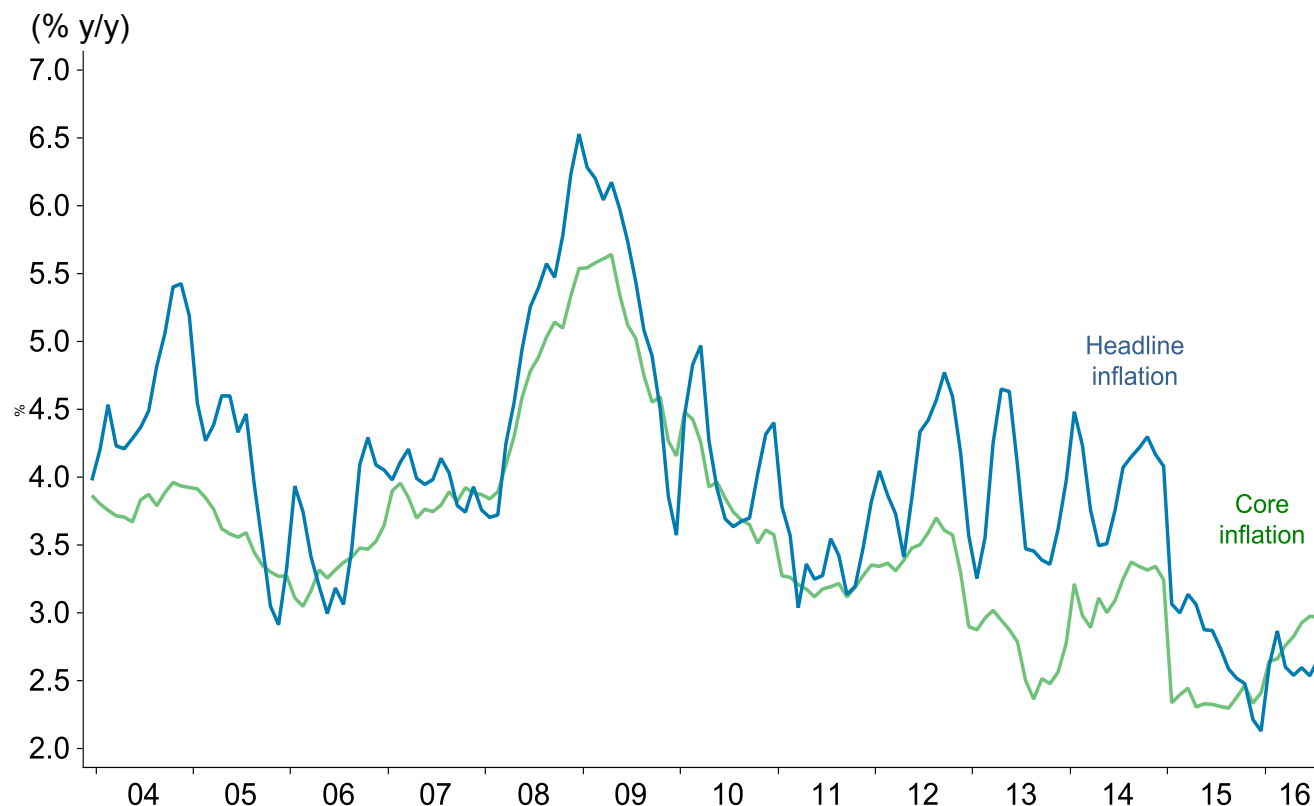
Soft US manufacturing is a risk to Mexico's growth



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MEXICO: INFLATION (%)



Source: Macrobond, Inegi, BNP Paribas



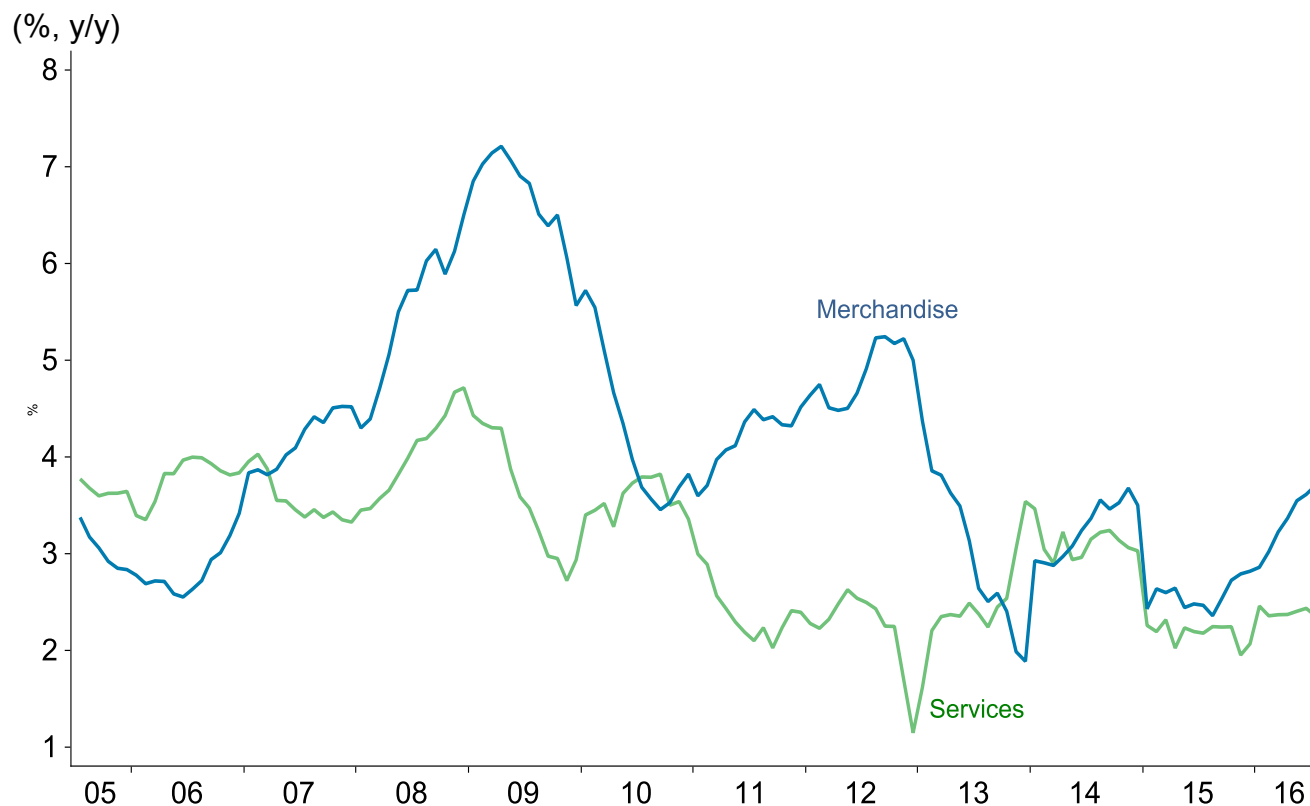
Inflation is rising towards the 3.0% target, while core overshoots headline



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MEXICO: CORE INFLATION BREAKDOWN (Y/Y, %)



Source: Macrobond, Inegi, BNP Paribas



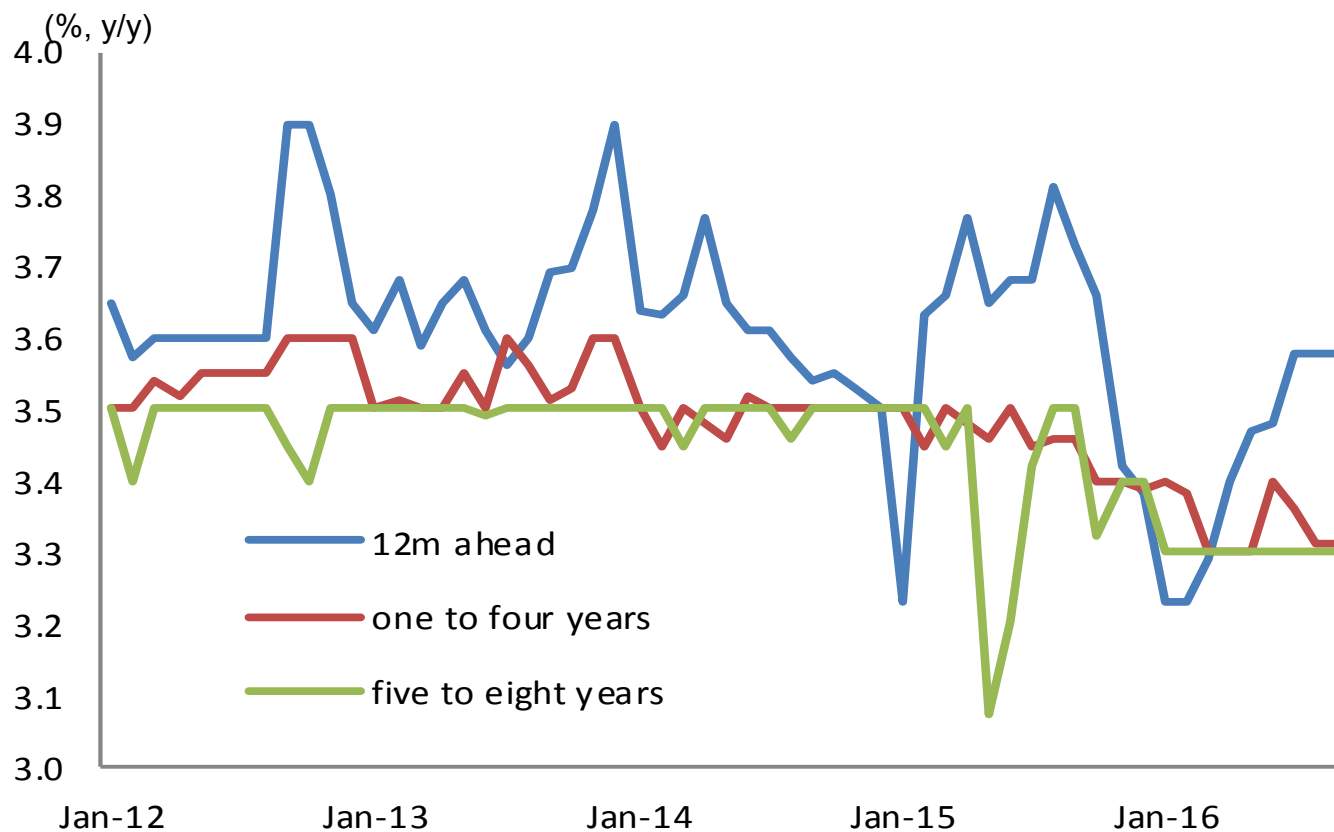
Within core inflation (ex food and energy), inflation in goods runs faster than in services



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MEXICO: INFLATION EXPECTATIONS



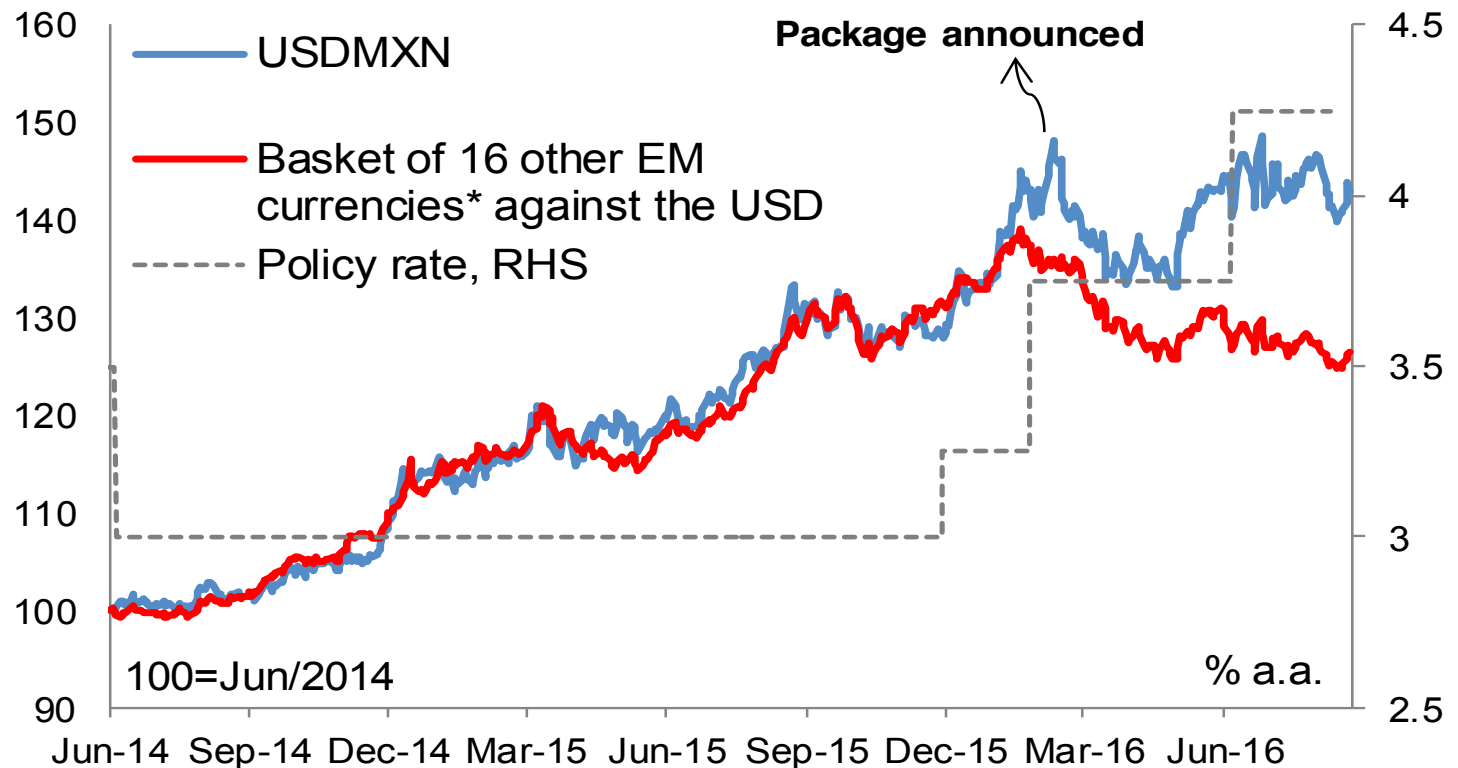
Long-run inflation expectations have shifted lower, but still above the 3.0% target



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MEXICO: USDMXN VS EM BASKET (JUNE 2014=100)



Source: Banxico, Bloomberg, BNP Paribas; *BRL, COP, CLP, PEN, CNY, RUB, TRY, KRW, ZAR, INR, PLZ, HUF, MYR, THB, IDR, PHP



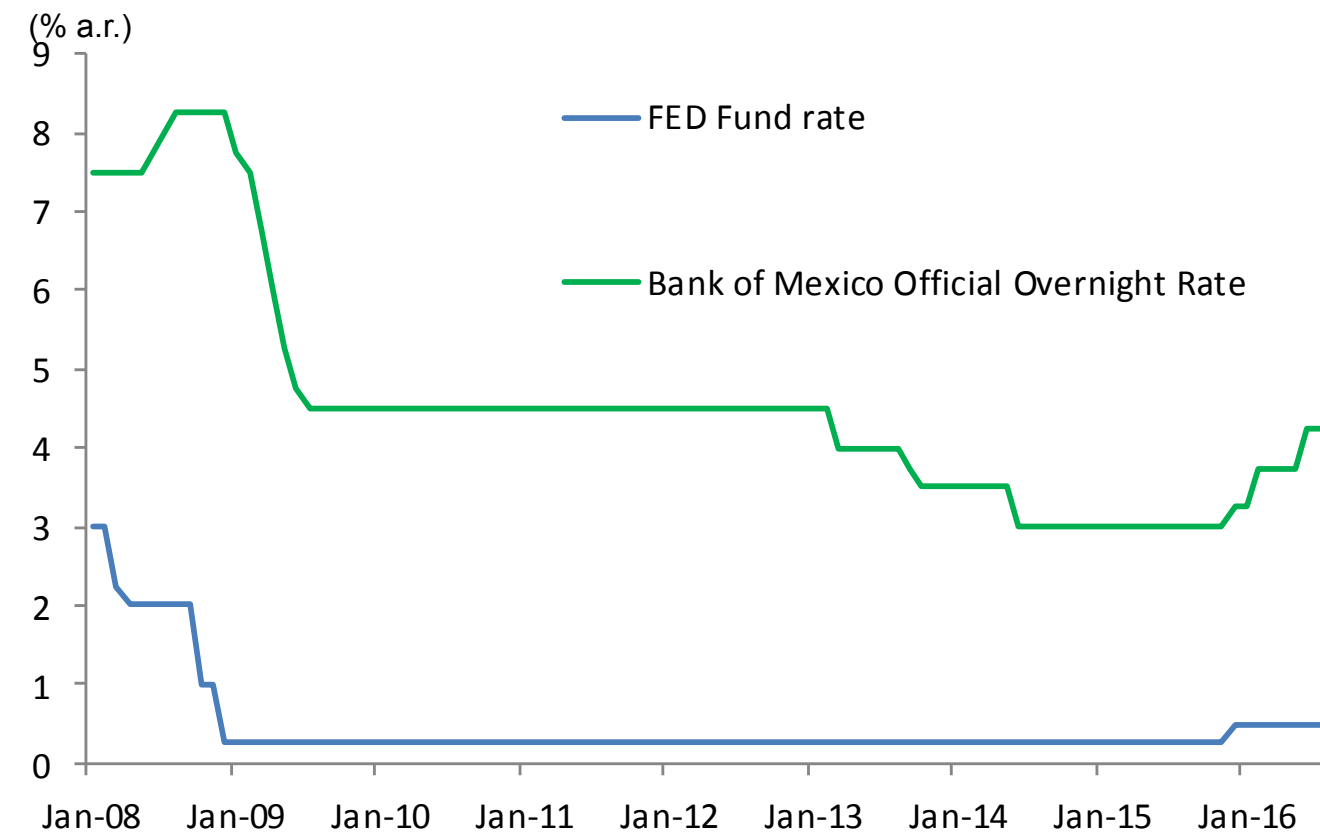
MXN's rapid divergence versus other EM currencies prompted policy rate action



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MEXICO: MONETARY POLICY



Source: Macrobond, Banxico, FED, BNP Paribas



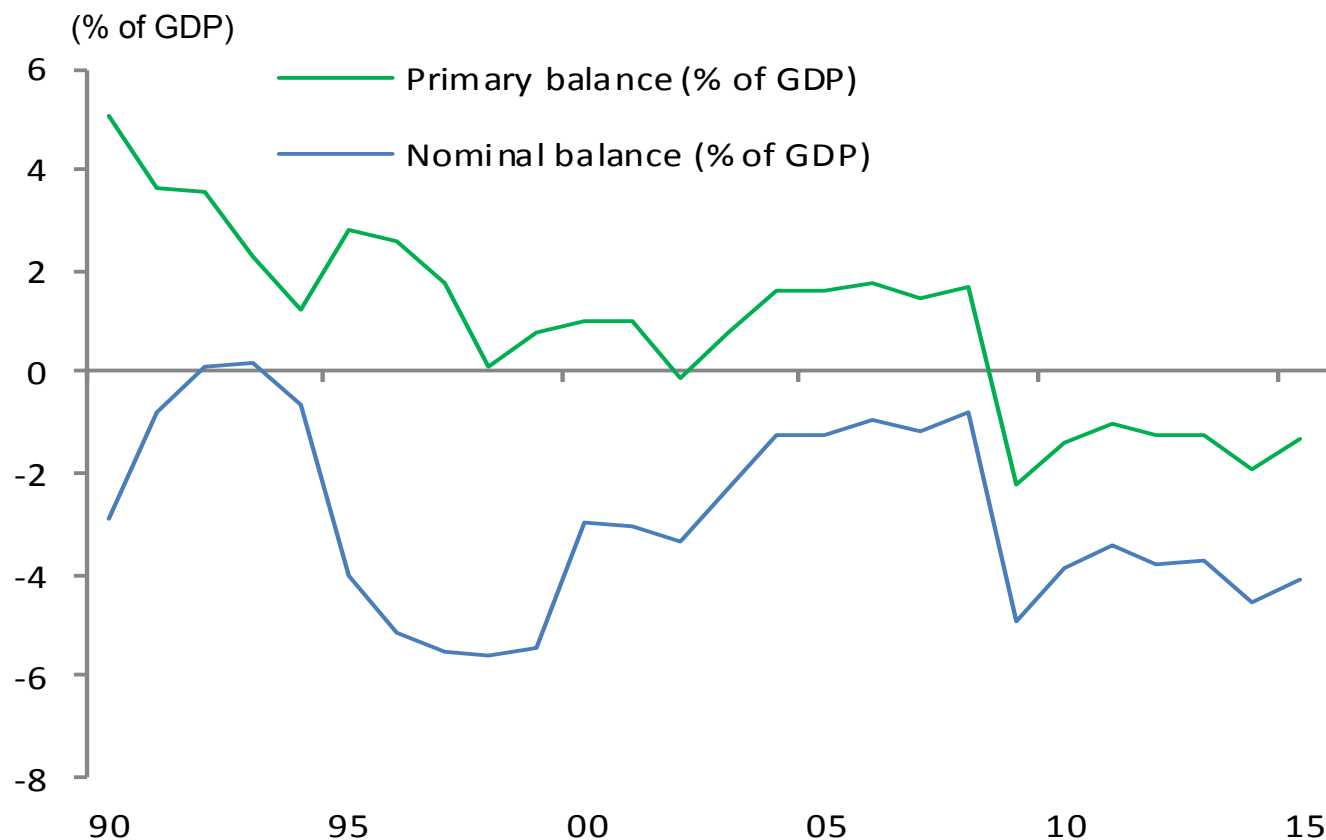
Banxico pays close attention to what the US Fed does



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MEXICO: FISCAL BALANCES (% OF GDP)



Source: Macrobond, IMF, FED, BNP Paribas



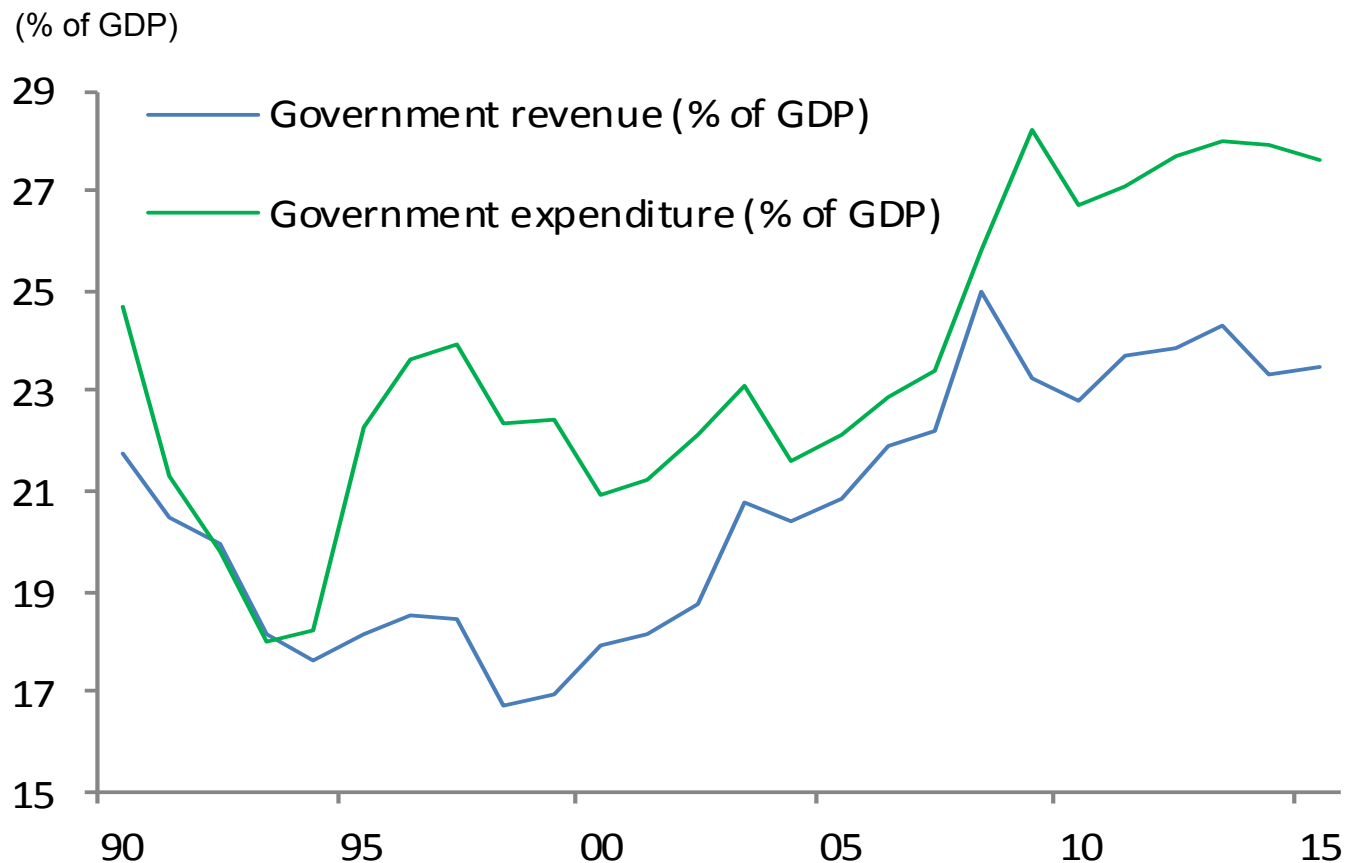
Fiscal balances need to improve in order to support debt dynamics



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MEXICO: FISCAL REVENUE AND SPENDING (% OF GDP)



Source: Macrobond, IMF, FED, BNP Paribas



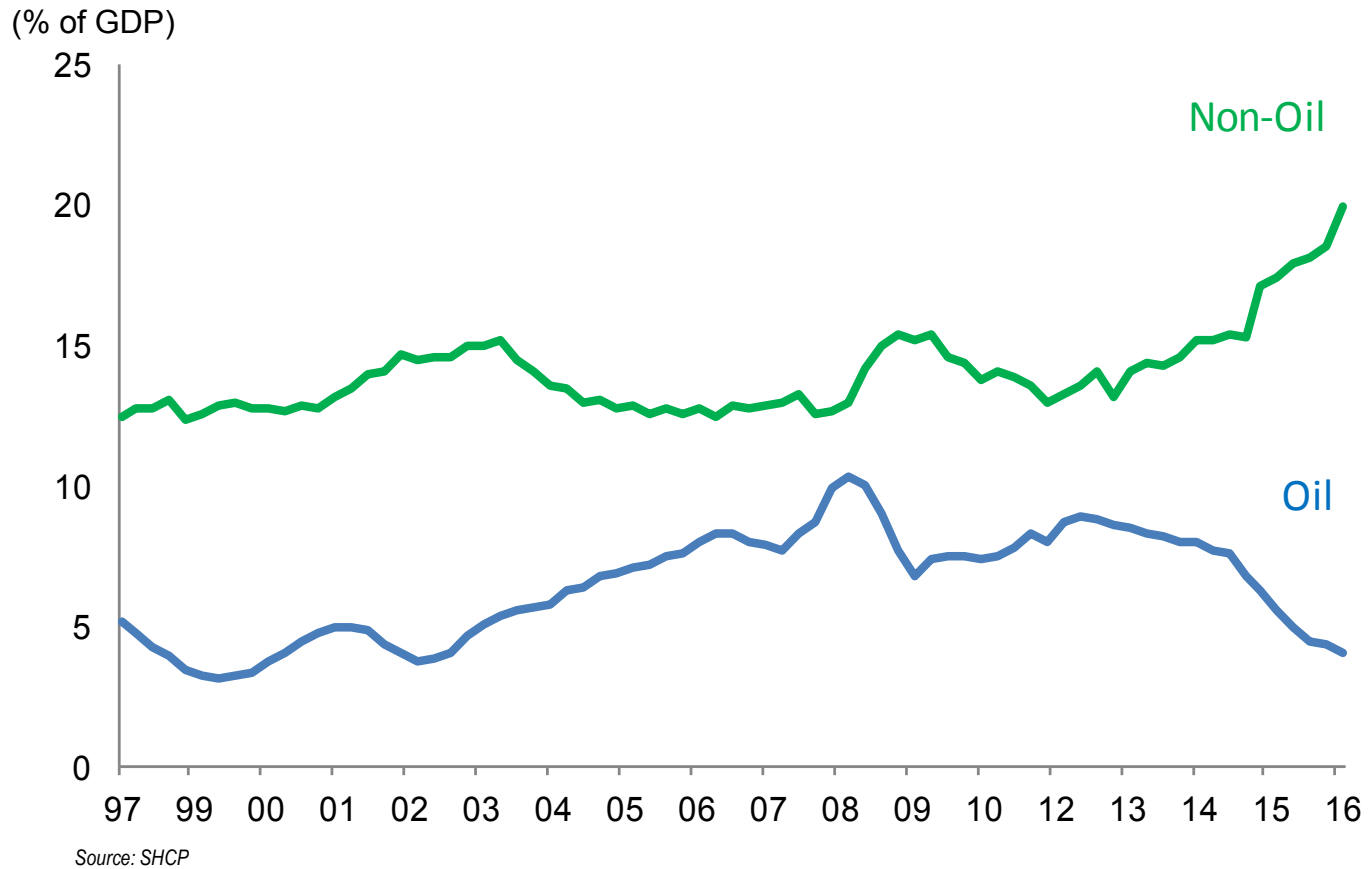
Spending has risen above revenues



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MEXICO: FISCAL REVENUE DEPENDENCE ON OIL IS SIGNIFICANT



Oil revenues are falling, while non-oil revenues have risen after the 2013 reforms

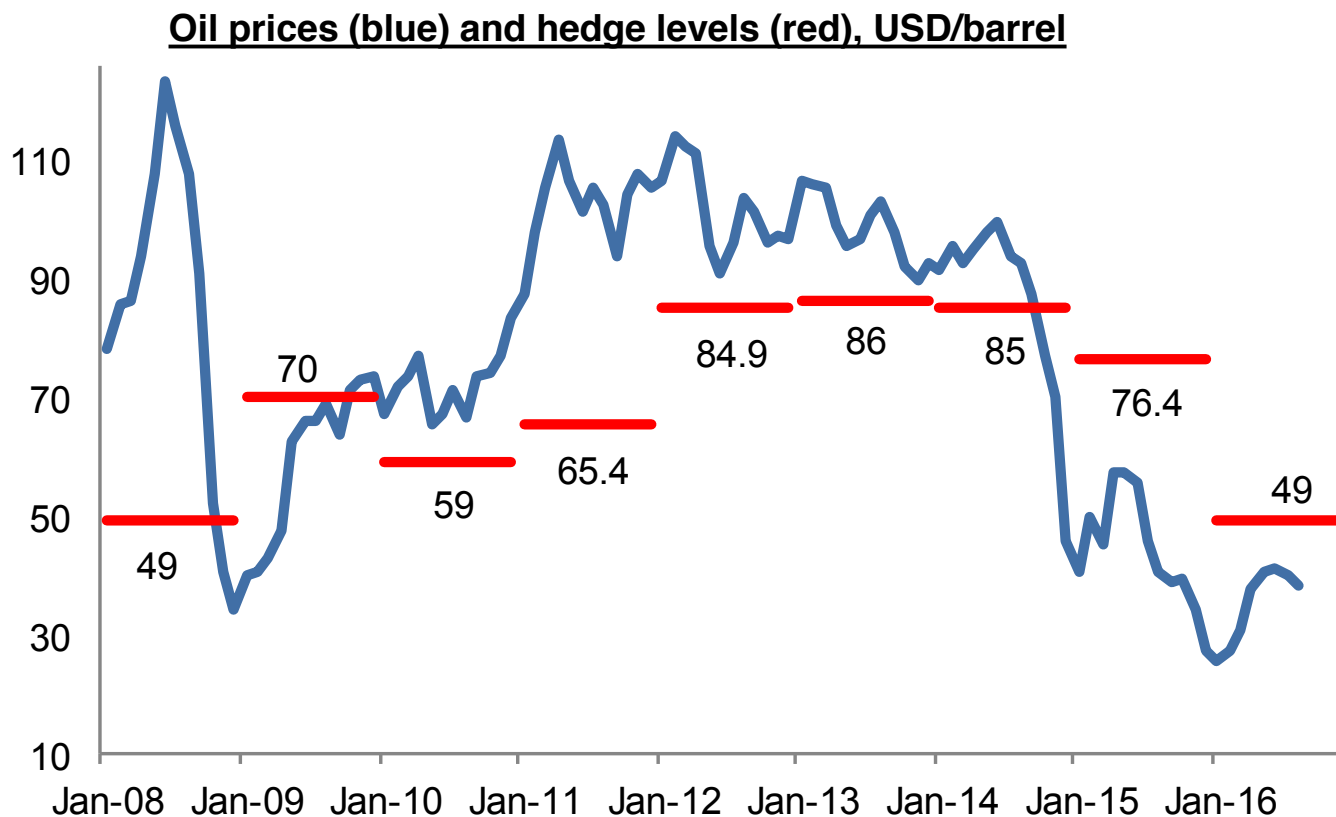


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MEXICO GRADE OIL PRICES AND HEDGE LEVELS (USD/BARREL)

- The government purchased put options at the cost of USD 1.1bn to hedge its 2016 oil revenue at USD 49/bbl.



Source: SHCP, Bloomberg, BNP Paribas



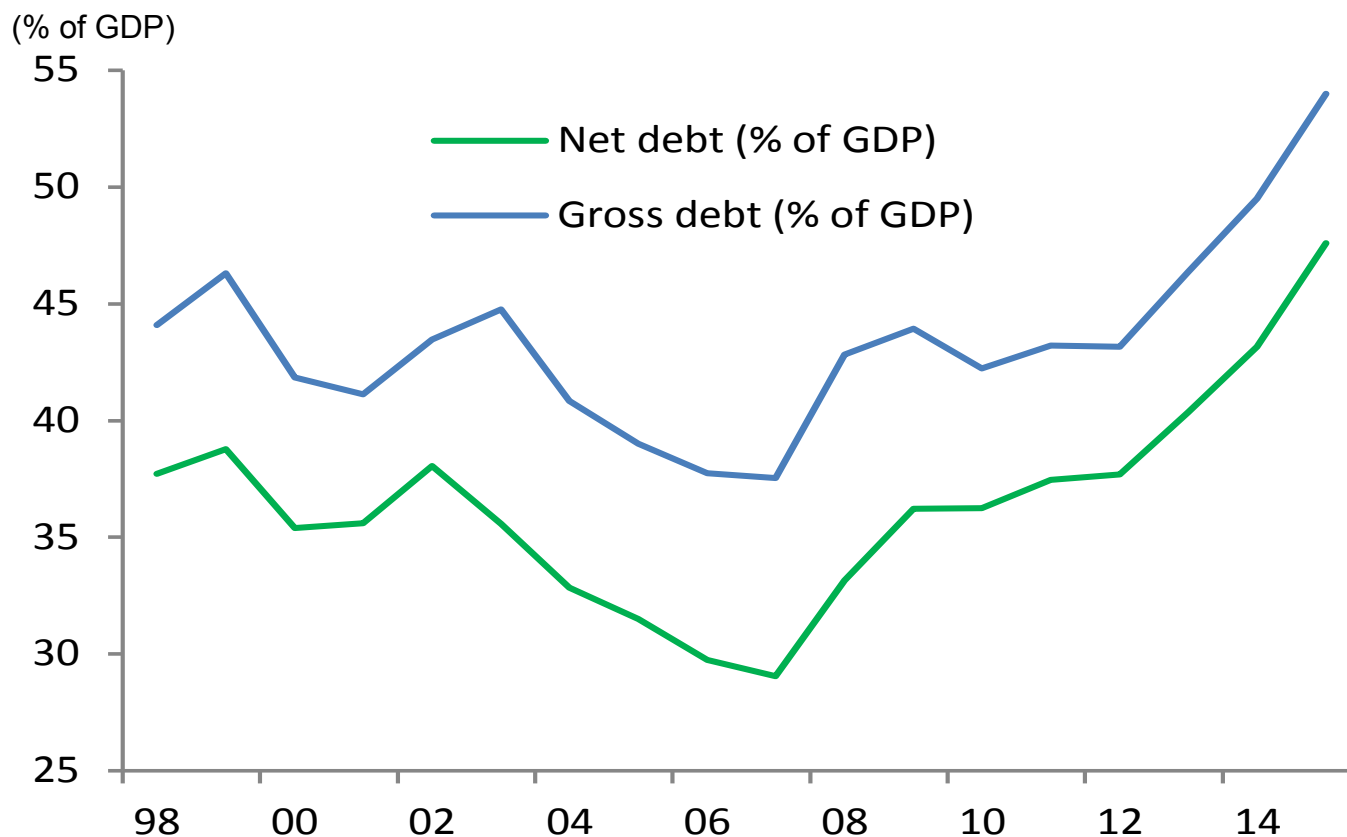
Hedging can help



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MEXICO: PUBLIC SECTOR DEBT (% OF GDP)



Source: Macrobond, IMF, FED, BNP Paribas



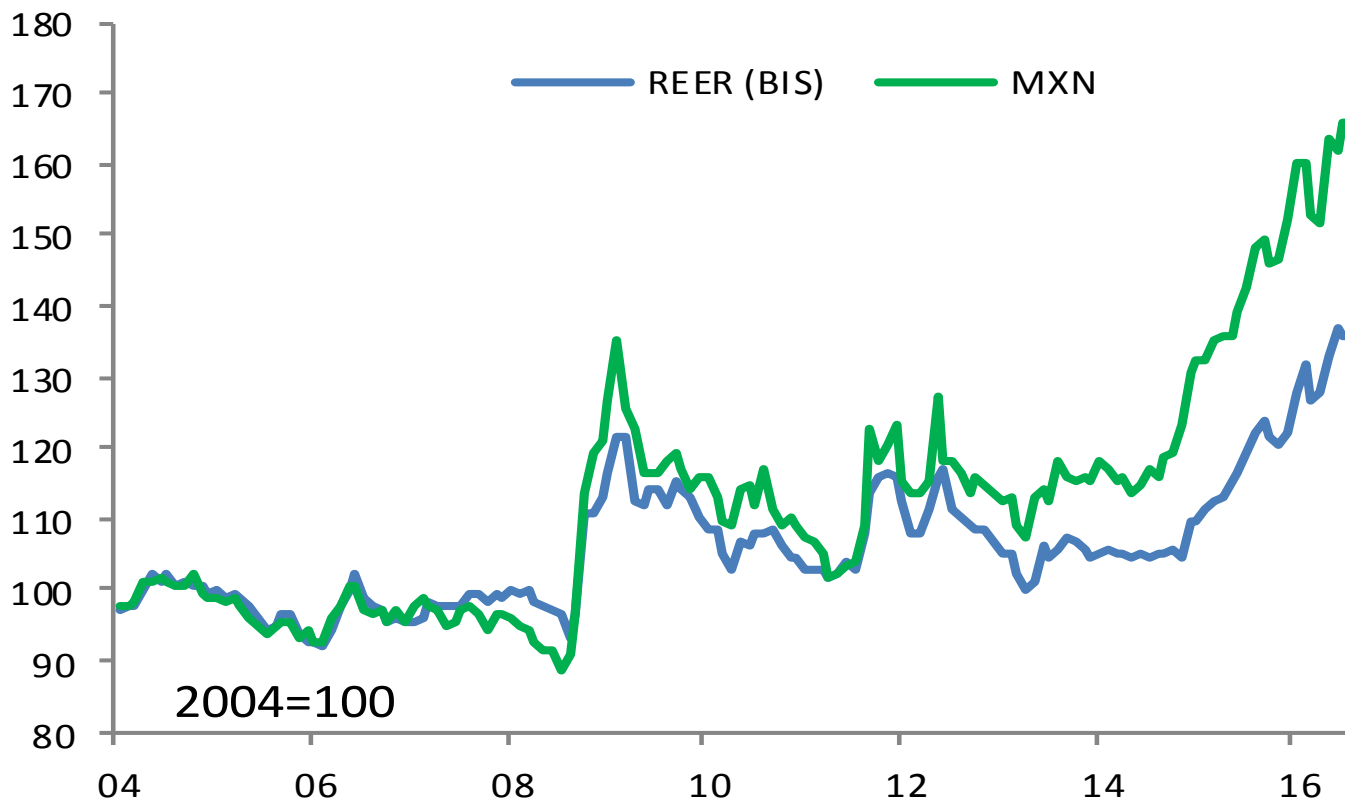
Debt has risen steadily in the last several years



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MEXICO: REER VS MXN



Source: Macrobond, BIS, BNP Paribas



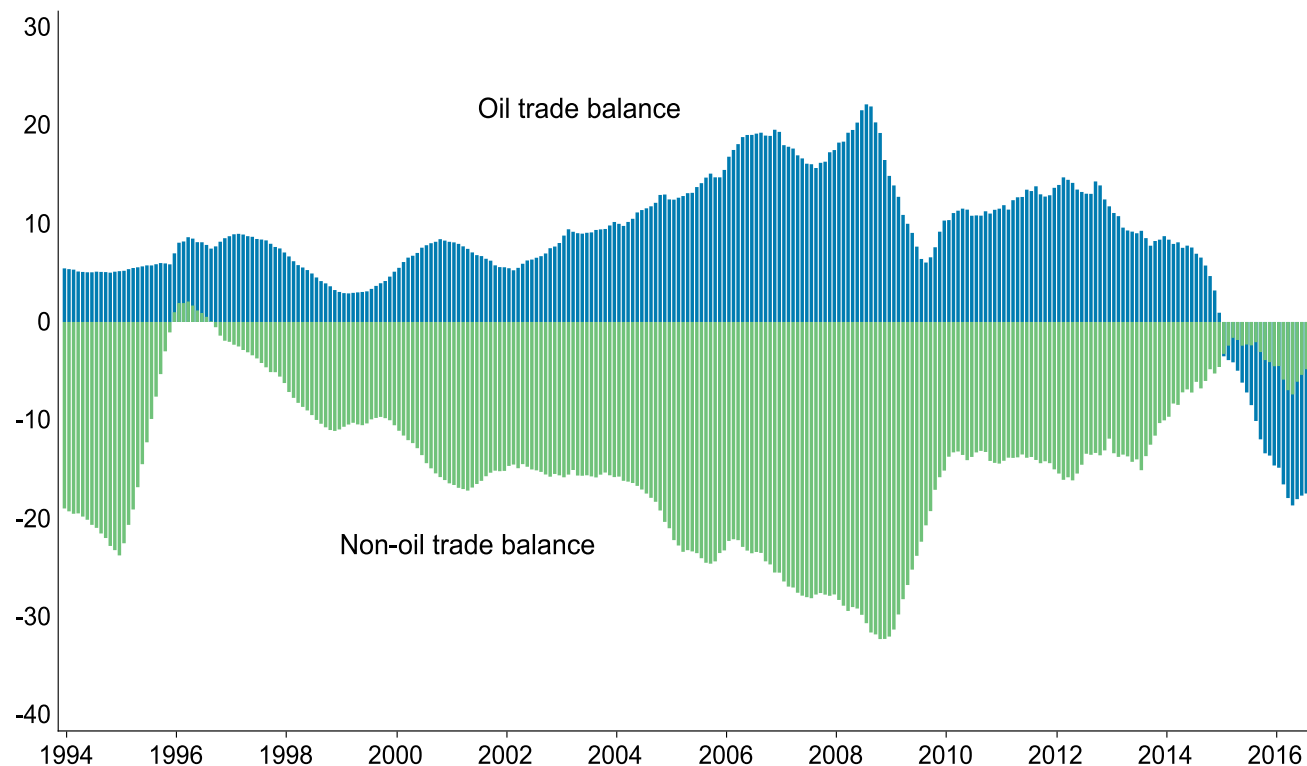
The currency has also weakened against a basket of currencies, adjusted for inflation



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MEXICO: TRADE BALANCE (12MMA, USD)



Source: Macrobond, Banxico, BNP Paribas



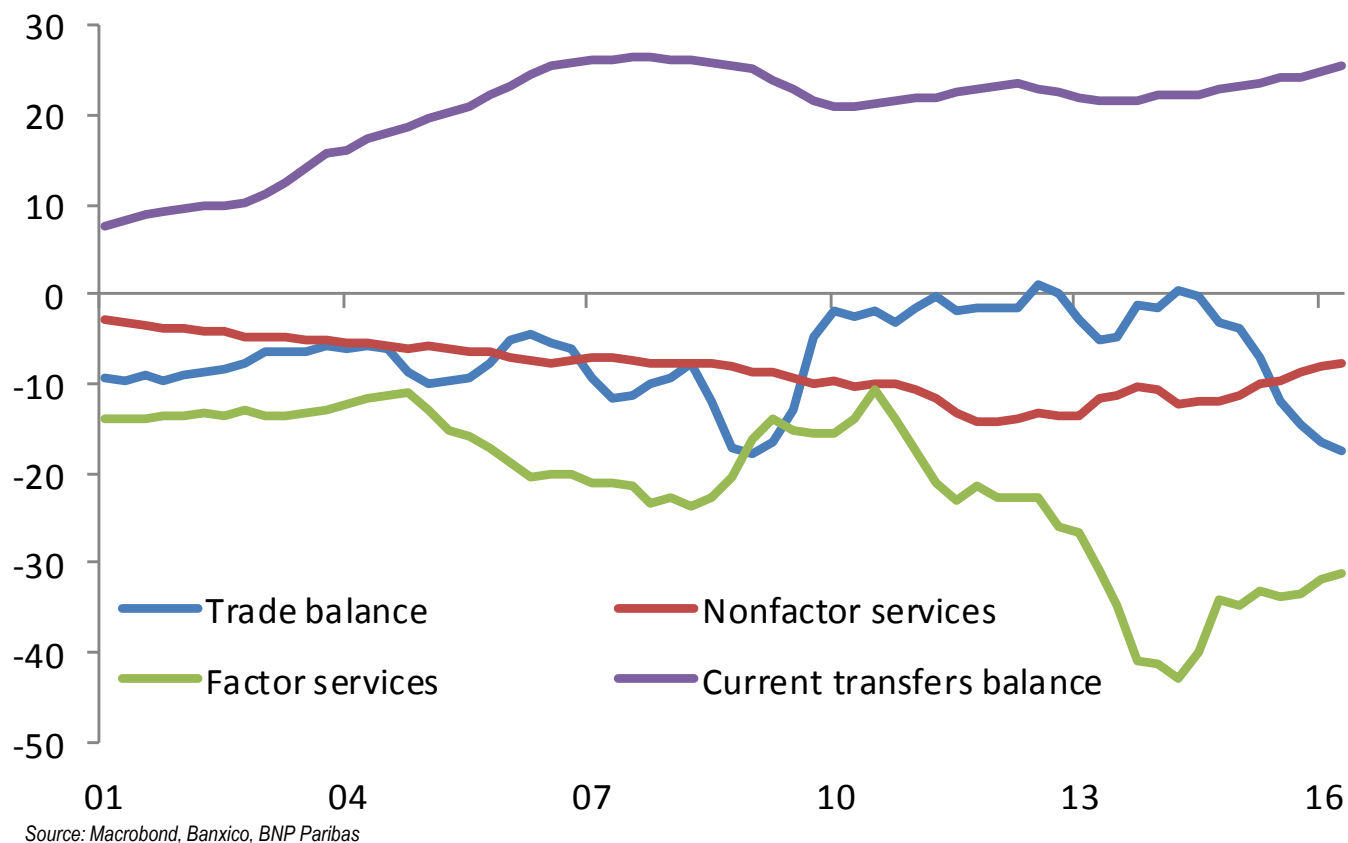
The oil trade balance has plunged into deficit, while the non-oil balance remains negative



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MEXICO: CURRENT ACCOUNT BREAKDOWN (USD BN, 12M SUM)



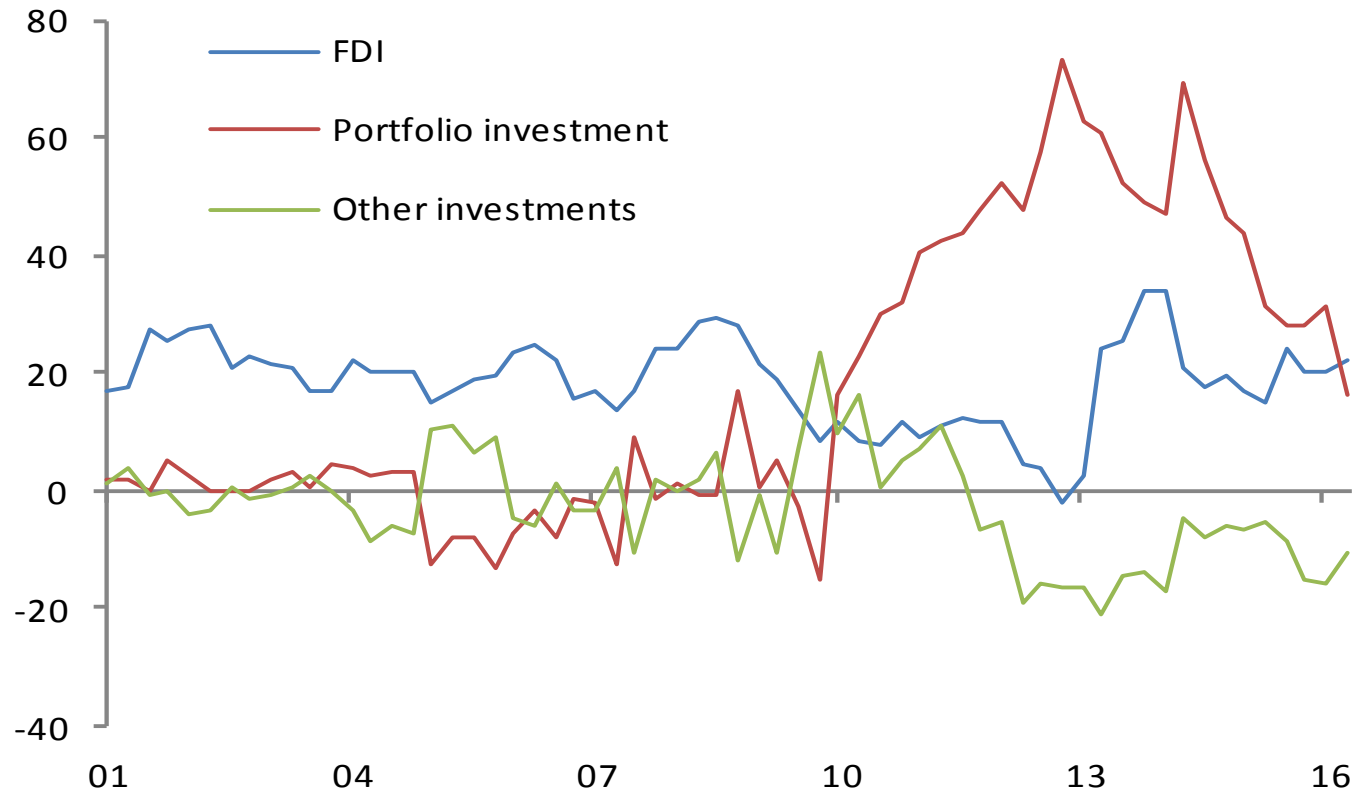
Transfers remain solid, while trade deficit has widened and services remain negative



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MEXICO: FINANCIAL ACCOUNT BREAKDOWN (USD BN, 12M SUM)



Source: Macrobond, Banxico, BNP Paribas



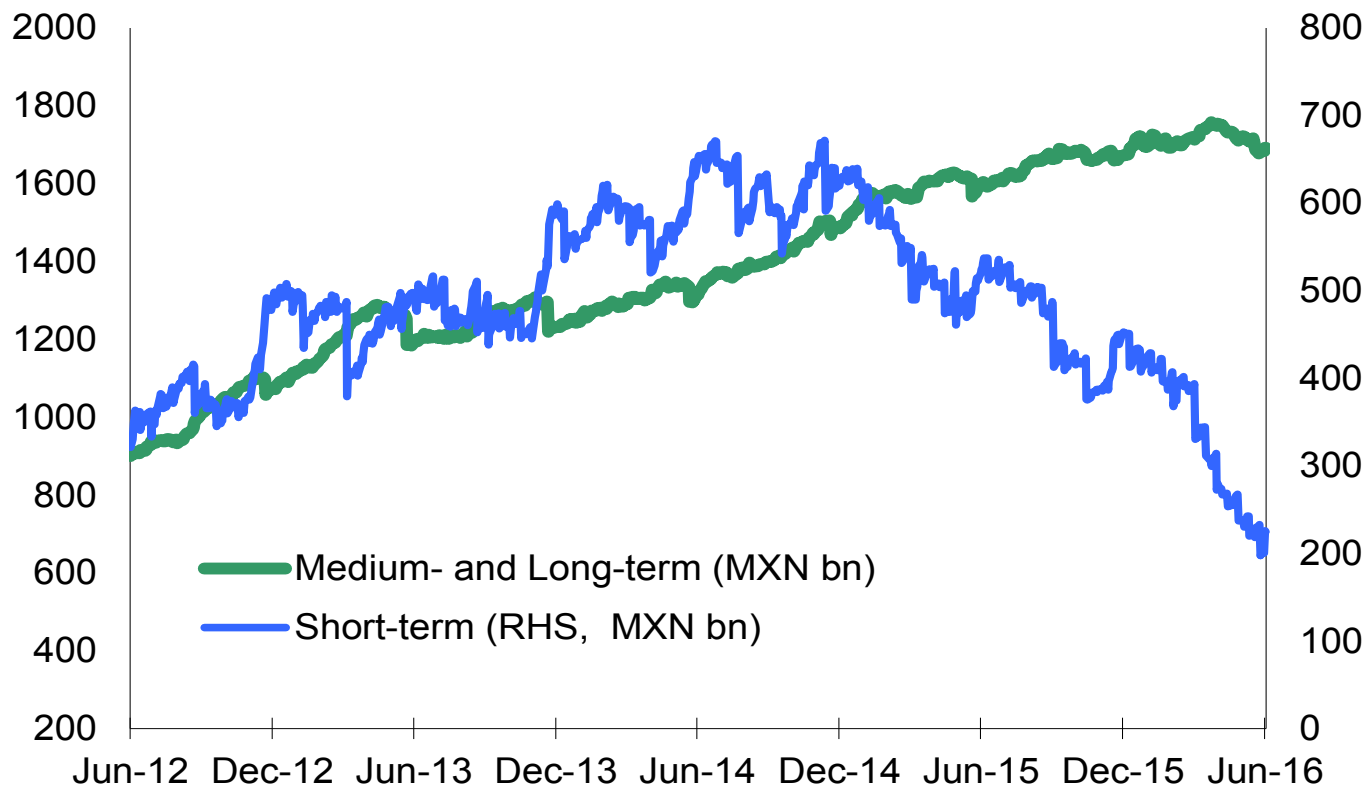
FDI has been relatively resilient, while other flows can prove volatile



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MEXICO: LOCAL DEBT HOLDINGS BY FOREIGN INVESTORS



Source: Banxico, BNP Paribas



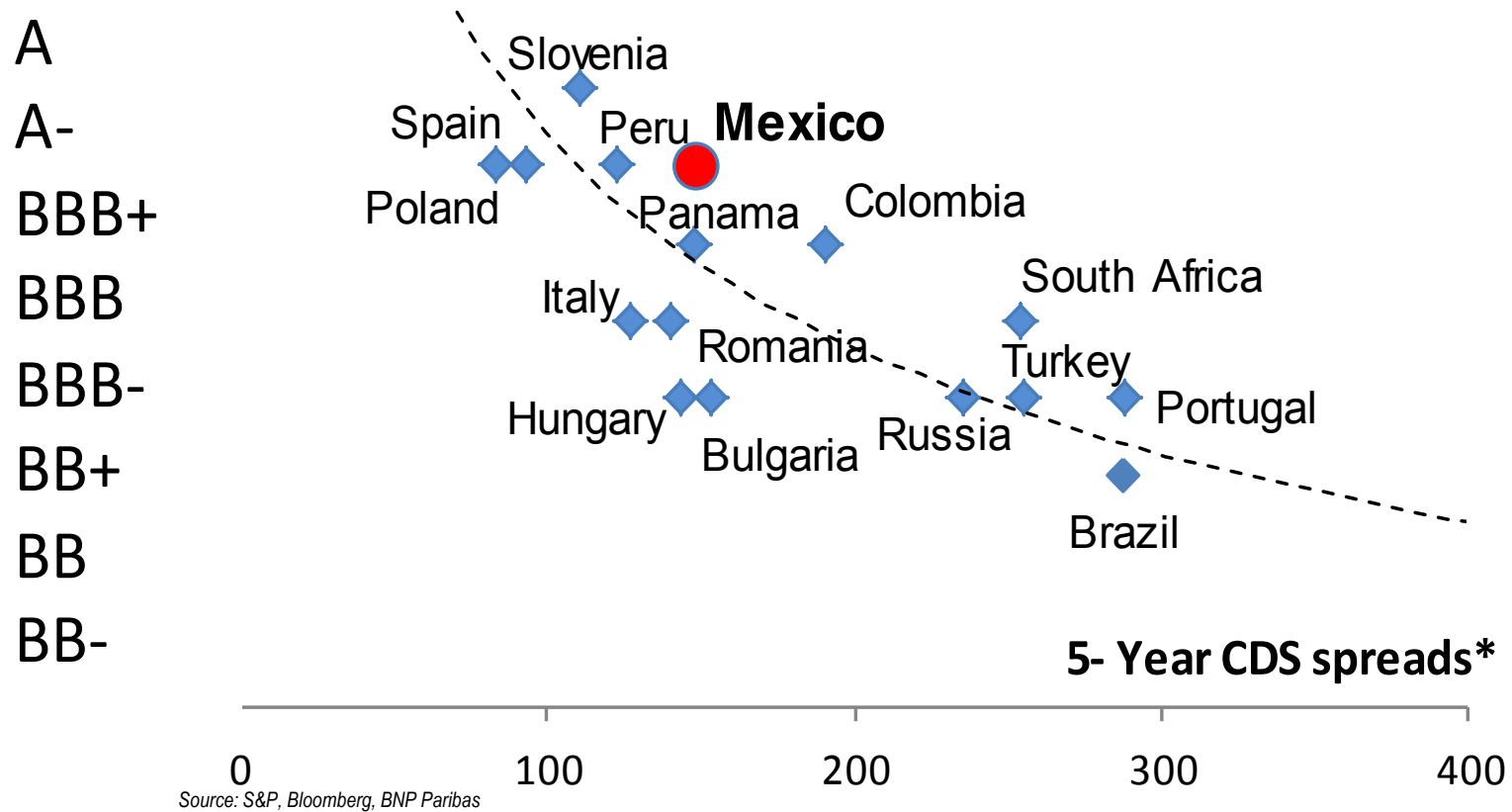
Foreign investment in Cetes has been pared back meaningfully



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MEXICO: STILL HIGHLY CREDIBLE



Sovereign ratings and CDS spreads tend to be correlated

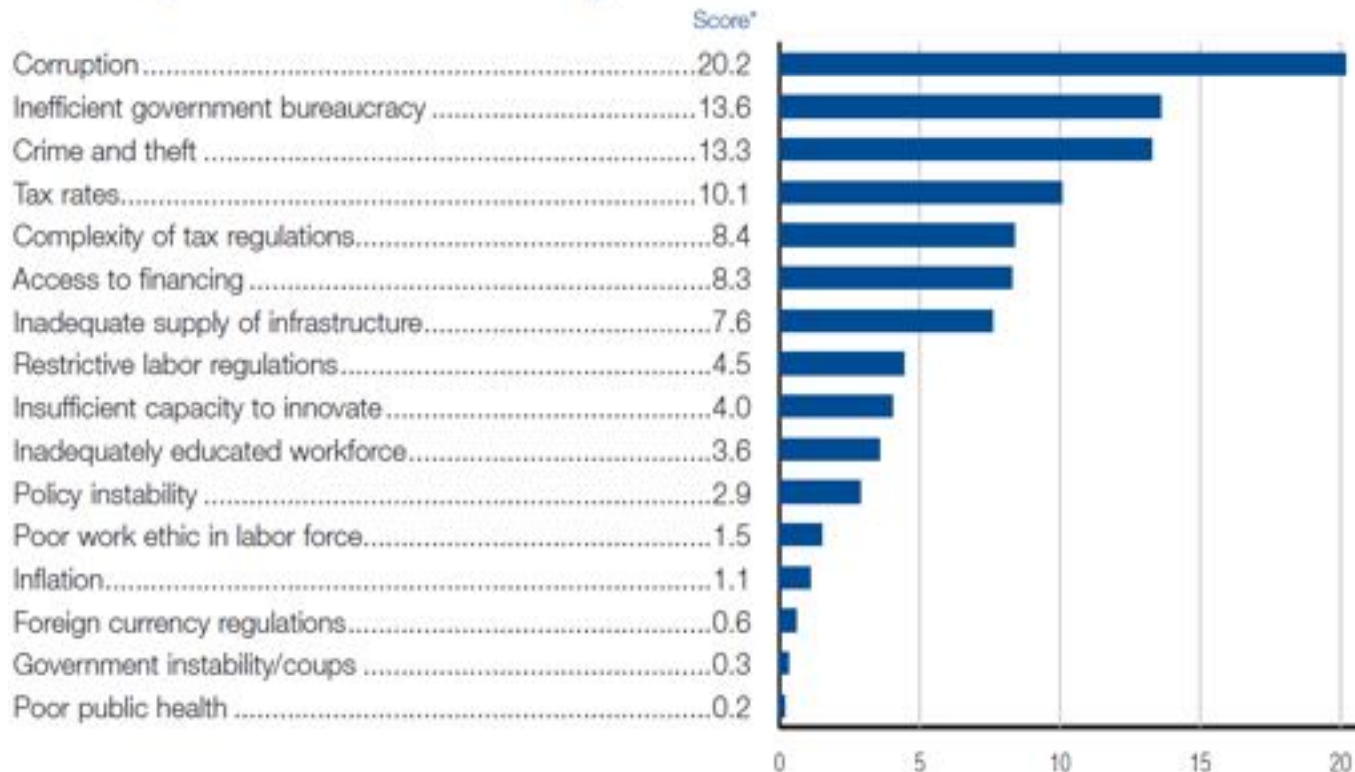


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MEXICO: STRUCTURAL REFORMS ARE NEEDED

The most problematic factors for doing business



Source: World Economic Forum- Doing Business Report 2016. Percentage of responses



Key issues to address: corruption, bureaucracy, crime and theft, taxes



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LATAM ECONOMIC FORECASTS

REAL GDP (% change)

	2014	2015	2016 (1)	2017 (1)
Latin America	0.9	-0.2	-0.6	2.6
Argentina	-2.6	2.4	-1.2	4.0
Brazil	0.1	-3.8	-3.0	2.0
Chile	1.9	2.0	1.5	2.0
Colombia	4.4	3.1	2.2	2.4
Mexico	2.2	2.5	2.0	2.9

INFLATION (% change in CPI, year end)

	2014	2015	2016 (1)	2017 (1)
Latin America	7.6	8.6	9.9	5.7
Argentina	23.7	15.0	43.0	18.0
Brazil	6.4	10.7	7.0	4.5
Chile	4.6	4.4	3.9	3.0
Colombia	3.7	6.8	6.1	4.0
Mexico	4.0	4.1	2.1	3.1

EXCHANGE RATE (domestic currency/US\$, year end)

	2014	2015	2016 (1)	2017 (1)
Argentina	8.47	12.93	16.00	17.50
Brazil	2.66	3.96	3.25	3.50
Chile	606	709	660	665
Colombia	2377	3175	2875	3300
Mexico	14.75	17.21	18.00	17.50

CURRENT ACCOUNT (% of GDP)

	2014	2015	2016 (1)	2017 (1)
Latin America	-3.2	-3.2	-2.2	-2.3
Argentina	-1.6	-2.7	-2.2	-2.3
Brazil	-4.4	-3.3	-1.0	-1.5
Chile	-1.2	-1.0	-1.9	-2.4
Colombia	-5.2	-6.4	-5.5	-4.6
Mexico	-1.8	-2.7	-3.0	-2.8

FISCAL BALANCE (% of GDP)

	2014	2015	2016 (1)	2017 (1)
Latin America	-4.0	-6.4	-6.5	-6.0
Argentina	-2.5	-5.3	-4.9	-4.5
Brazil	-6.2	-10.3	-10.1	-9.4
Chile	-1.6	-2.2	-3.2	-2.8
Colombia	-2.6	-3.1	-4.0	-3.4
Mexico	-2.3	-3.1	-3.5	-3.0

INTEREST RATE (benchmark, year end)

	2014	2015	2016 (1)	2017 (1)
Argentina	21.00	25.00	22.00	17.00
Brazil	11.75	14.25	13.25	9.25
Chile	3.00	3.50	3.50	4.00
Colombia	4.50	5.75	7.75	5.50
Mexico	3.50	3.00	3.25	4.50

Source: BNP Paribas Latam Economic Research



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GLOBAL OUTLOOK: CURRENCIES

FX Forecasts (end quarter)

USD Bloc	Spot	Q3 '16	Q4 '16	Q1 '17	Q2 '17	Q3 '17	Q4 '17
EURUSD	1.12	1.07	1.10	1.12	1.10	1.07	1.05
USDJPY	103.61	111	108	108	112	115	118
USDCHF	0.98	1.07	1.05	1.05	1.09	1.12	1.14
GBPUSD	1.33	1.24	1.31	1.34	1.35	1.36	1.37
USDCAD	1.31	1.40	1.40	1.40	1.37	1.35	1.35
AUDUSD	0.75	0.70	0.67	0.67	0.66	0.66	0.65
NZDUSD	0.73	0.66	0.65	0.65	0.64	0.64	0.63
USDSEK	8.58	8.41	8.09	7.86	7.91	8.13	8.29
USDNOK	8.35	8.79	8.55	8.30	8.36	8.50	8.57

LATAM Bloc	Spot	Q3 '16	Q4 '16	Q1 '17	Q2 '17	Q3 '17	Q4 '17
USDARS	14.91	15.20	16.00	16.25	16.35	16.70	17.50
USDBRL	3.26	3.20	3.25	3.40	3.45	3.50	3.50
USDCLP	681.10	670	660	660	650	660	665
USDMXN	18.89	18.60	18.00	17.85	17.75	17.65	17.50
USDCOP	2979	2900	2875	2925	2950	3025	3300
USDPEN	3.40	3.35	3.30	3.35	3.25	3.35	3.40

Source: BNP Paribas



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