

Mexico City, April 1st, 2016

THE MINISTRY OF FINANCE SUBMITS THE GENERAL ECONOMIC POLICY PRELIMINARY GUIDELINES FOR 2016 TO CONGRESS

- *The General Economic Policy Preliminary Guidelines document for 2016 is based on realistic premises, considering an adverse external environment, and foresees the accomplishment of the public finances objectives of the Economic Program for 2016.*
- *The Federal Government will maintain a policy of no tax increases and will not resort to higher indebtedness, against the prospects of lower oil revenues. Therefore, the Government will make the necessary fiscal adjustments to maintain solid public finances.*
- *The Historical Balance of Public Sector Borrowing Requirements (HBPSBR), the broadest measure of fiscal debt, is estimated to start a declining trajectory at the beginning of 2017, one year ahead of last year's projections.*
- *To comply with the fiscal consolidation trajectory in 2017, the Government foresees an adjustment of programmable expenditure, excluding high economic and social impact investment, for Ps. 175.1 billion in addition to the preemptive expenditure adjustment announced in February of Ps. 132.3 billion. Estimates of public finances in the General Economic Policy Preliminary Guidelines does not consider the use of surplus resources, such as the operating surplus of Banco de México.*

The Ministry of Finance and Public Credit complies with the timely submission to Congress of the "Document relative to the compliance with dispositions in Article 42, Fraction I, of the Federal Budget and Fiscal Responsibility Law", commonly known as "General Economic Policy Preliminary Guidelines".

As in 2015, this year's General Economic Policy Preliminary Guidelines are presented within an adverse external environment. In addition, some risks have materialized or intensified during the last months. The environment in 2016 is characterized by episodes of high volatility in financial markets, steep falls in commodity prices,

monetary policy divergence in advanced economies, uncertainty about the growth pace of emerging economies and possible economic consequences in the face of intensifying geopolitical conflicts.

Despite this adverse environment, the Mexican economy has set itself apart from other emerging economies in Latin America and comparable emerging economies in other regions. Among the main differentiating factors are the strengthening of tax revenues, efficient and responsible management of public debt, a credible monetary policy with well anchored inflation expectations, a flexible exchange rate, an adequate level of international reserves, as well as access to the Flexible Credit Line from the International Monetary Fund, and a hedging strategy for oil revenues, which generated more than USD 6.3 billion in revenues in 2015. The public balance objectives were accomplished in 2015. The Public Sector Borrowing Requirements (PSBR), the broadest measure of public deficit, reached a level of 4.1% of GDP, a decrease of 0.5% compared to that observed in 2014.

To preserve and complement the strengths of the Mexican economy, given the deterioration of the external environment, and in order to preserve economic stability, on February 17th, 2016, the Ministry of Finance and Banco de Mexico announced preventive, integral and coordinated fiscal, monetary and foreign exchange policies. Among the measures, the Ministry of Finance announced a preemptive adjustment in the Federal Public Administration for 2016, amounting to Ps.132.3 billion, equivalent to 0.7% of GDP. Additionally, Banco de Mexico increased 50 basis points the target for the Overnight Interbank Rate, to 3.75%, and the Foreign Exchange Commission suspended dollar auctions and introduced the possibility of discretionary interventions in the exchange market under exceptional conditions.

For 2016, an updated macroeconomic framework is presented according to the new global economic environment. Estimates of public finances are consistent with the balance goals approved by Congress for 2016 (a budgetary deficit equivalent to 0.5% of GDP and 3.0% of GDP, considering investment in projects with high economic and social impact, as well as the PSBR of 3.5% of GDP). Considering the deterioration of the external environment, it is proposed to use for public finances estimates an oil price of 25 dollars per barrel (dpb) and a production platform of 2,123 thousand barrels per day (Mb/d).

For 2017, the economic growth forecast is between 2.6% and 3.6%, and budgetary revenues are projected using realistic and responsible assumptions. In particular, an oil price of 35 dpb is proposed, consistent with the projections of the futures market. It is also considered an oil production platform of 2,028 Mb/d, consistent with Pemex's

estimates and the permanent expenditure adjustment of Ps. 100 billion of the company.

The projected reduction for revenues as a result of the macroeconomic framework and the commitment to the decreasing trajectory of the deficit, implies the need of an adjustment to programmable expenditure, excluding high economic and social impact investment, of Ps. 311.8 billion compared to the 2016 Federal Budget. Thus, considering the preemptive adjustment of expenditure announced in February of Ps. 132.3 billion (2017 Ps. 136.7 billion), an additional adjustment of Ps.175.1 billion will be required. The amount of the adjustment in the projected expenditure is mainly explained by a lower deficit at Ps. 99.9 billion, lower budgetary revenues by Ps. 118.2 billion and a higher non-programmable expenditure by Ps. 93.7 billion.

Therefore, it is estimated that the HBPSBR will initiate a downward trend in 2017, consistent with the fiscal consolidation effort in place. The path presented in the General Economic Policy Preliminary Guidelines does not consider the use of surplus resources, such as the operating surplus of Banco de México.

The Economic Program for 2016 allowed to identify opportunity areas in the budget; and with the creation of new instruments for investment in infrastructure, it will be possible to make the necessary adjustments and maintain a significant flow of investment in strategic sectors. Consequently, Mexico has the space and tools to make adjustments without damaging economic growth while maintaining the commitment to not increase public debt or raise taxes.

ANNEX I

MACROECONOMIC FRAMEWORK, 2016-2017 ^e		
	2016	2017
Gross Domestic Product		
Real % growth (range)	2.6 – 3.6	2.6 – 3.6
Nominal (billion pesos)*	19,203.9	20,432.4
GDP deflator	3.2	3.3
Inflation		
Dec. / Dec.	3.0	3.0
Nominal exchange rate		
End of period	17.5	17.0
Average	18.0	17.2
Interest rate (28-days Cetes)		
Nominal, end of period, %	4.3	5.3
Nominal average, %	3.7	4.8
Real accumulated, %	0.8	1.8
Current account		
Million dollars	-33,067.8	-34,429.8
% of GDP	-3.1	-2.9
Supporting variables:		
Fiscal balance, % of GDP		
With high impact investment	-3.0	-2.5
Excluding high impact investment	-0.5	0.0
United States GDP		
Real % growth	2.1	2.4
United States industrial production		
Real % growth	0.9	2.4
United States inflation		
Average	1.3	2.3
International interest rate		
3-month LIBOR (average)	0.7	1.1
FED Funds Rate (average)	0.5	0.7
Oil (Mexican mix)		
Average price (dpb)	25	35
Average production platform (Mb/d)	2,123	2,028
Average export platform (Mb/d)	968	873
Gas		
Average price (dollars/million Btu)	2.0	2.6

* Corresponds to the point scenario used in the estimation of public finances.
e/Estimation.

ANNEX II

Estimation of public finances for 2016-2017					
	Millions of current pesos		% del PIB		Real growth %
	2016 Approved	2017 Estimation	2016 Appr.	2017 Estim.	
Economic balance	-577,192.0	-510,810.0	-3.0	-2.5	-14.3
(Excluding high-impact investment)	-96,703.2	0.0	-0.5	0.0	-100.0
Non-budgetary balance	0.0	0.0	0.0	0.0	n. s.
Budgetary balance	-577,192.0	-510,810.0	-3.0	-2.5	-14.3
Budgetary revenues	4,154,633.4	4,173,568.7	21.6	20.4	-2.8
Oil	884,439.6	686,451.1	4.6	3.4	-24.9
Non-oil	3,270,193.8	3,487,117.5	17.0	17.1	3.2
Federal Government	2,616,393.5	2,825,513.8	13.6	13.8	4.5
Tax	2,407,205.9	2,651,790.1	12.5	13.0	6.6
Non-tax	209,187.6	173,723.7	1.1	0.9	-19.6
PEDBC's	653,800.3	661,603.8	3.4	3.2	-2.0
Paid net expenditures	4,731,825.4	4,684,378.7	24.6	22.9	-4.2
Paid programmable	3,574,657.0	3,395,285.1	18.6	16.6	-8.1
Payment deferrals	-31,085.0	-32,110.8	-0.2	-0.2	0.0
Accrued programmable	3,605,742.0	3,427,395.9	18.8	16.8	-8.0
Non programmable	1,157,168.4	1,289,093.6	6.0	6.3	7.8
Financial cost	462,372.5	551,124.7	2.4	2.7	15.4
Non-earmarked transfers	678,747.3	706,978.9	3.5	3.5	0.8
Adefas	16,048.6	30,990.0	0.1	0.2	86.9
Primary economic surplus	-114,319.6	40,814.7	-0.6	0.2	n.a.

--- 0 ---