

Mexico City, February 17th, 2016.

PREEMPTIVE FISCAL ADJUSTMENT STRENGTHENS THE COMMITMENT TO MACROECONOMIC STABILITY

- **The Federal Government announces a preemptive spending adjustment in the Federal Public Administration for 2016 that amounts to 132.3 billion pesos, 0.7% of GDP, to face deteriorating conditions in the global environment.**
- **The preemptive adjustment consists of a reduction in federal government spending for 2016 by 32.3 billion pesos and a 100 billion pesos adjustment in PEMEX current fiscal year budget, which will be proposed by its CEO to the Board of Directors next week.**
- **The adjustment of the Federal Government agencies focuses on current expenditure that accounts for 60% of the total. The adjustment does not affect security areas or programs of the Ministry of Social Development (SEDESOL).**
- **The Federal Government adjustment is consistent and supports the measures proposed by PEMEX to address the structural challenges of the new oil order.**

Since the beginning of 2016, volatility in international financial markets has increased, mainly associated with a further drop in oil prices, the process of rising interest rates in the US and downside risks in the global economy, particularly in China.

In this context, the Government has acted with fiscal responsibility, meeting the established metrics of fiscal balance and acting in coordination with Banco de Mexico. As a result, the performance of Public Sector Borrowing Requirements, the broadest measure of fiscal balance, which includes PEMEX, fell by 0.5% of GDP to close at 4.1% of GDP during 2015, consistent with the approved target.

The government policy responses promoted, in a context of volatility and widespread appreciation of the dollar, an orderly adjustment in financial variables and an environment in which Mexico's growth rate accelerated in 2015 to reach

2.5%. Excluding oil-related activities, growth is estimated at 3.2%. This internal growth dynamic explains the creation of 644 thousand new formal jobs in 2015.

By 2016, the Congress approved a responsible budget, which priority is to preserve stability and reduce the deficit by another 0.5% of GDP. The Budget for 2016 also approved an amendment to the Federal Budget and Fiscal Responsibility Law (LFPRH) to ensure transparency and predictability over the responsible use of revenues from the operating surplus of Banco de Mexico.

The oil price hedges obtained for fiscal year 2016 protect the level of budgetary revenues this year and thus, the government can continue on the path of the committed multiannual consolidation of public finances. However, given the volatility of the external environment, it is necessary to take additional measures for three reasons:

1. The depreciation of the exchange rate, partly, reflects the fall in oil prices which worsened Mexico's terms of trade. In face of this environment, it is necessary that external shocks are addressed in a comprehensive and coordinated manner through the use of all instruments, avoiding that all the adjustments are given only through a single instrument or variable.
2. The oil hedges protect revenues of the government for 2016, but not for 2017. Therefore, given the recent evolution in oil prices, it is appropriate to implement a preemptive fiscal adjustment to achieve the goals set for fiscal consolidation in 2017.
3. PEMEX should use of all the instruments the Energy Reform has provided, to operate more efficiently, increasing profits in benefit of the economy. The effort must focus on PEMEX since it is not only facing a drop on its revenues, but also must redefine its business strategy in a new context of low prices and a new institutional framework.

For these reasons, the Government has doubled efforts required to further strengthen public finances, by adjusting spending, complying with the promise of not increasing taxes or introducing new ones, and without increasing public debt.

Therefore, the preemptive spending cut in the Federal Public Administration for 2016 amounts to 132.3 billion pesos, 0.7% of GDP. This amount includes the adjustment of 100 billion pesos in PEMEX, according to what the CEO of the

state productive enterprise has informed to the Ministry, which will be submitted for approval to the Board of Directors.

The preemptive adjustment of the Federal Government, which includes the Federal Electricity Commission (CFE), amounts to 32.3 billion pesos (0.2% of GDP), of which 60% is from current expenditure and 40% is from investment expenditure. 91% of the adjustment is from the Federal Government agencies. The remaining 2.5 billion is from the Federal Electricity Commission, which will also be submitted for approval to its Board of Directors.

The adjustment in terms of investment considered the profitability and social impact of each project; the pace of implementation, and which ones already have the technical and legal elements to initiate implementation, such as the record of the investment portfolio that the Ministry of Finance manages and integrates. As a result, the governmental agencies must, in some cases, reduce and reschedule goals of the programs and investment projects approved for this year.

The preemptive adjustment does not modify any national security program or the budget allocated to the Ministry of Social Development (SEDESOL).

The CEO of PEMEX has informed the Ministry, that a proposal to adjust spending will be submitted to the Board of Directors for approval. The adjustment program prioritizes actions that will provide liquidity during 2016 and strengthen its long-term solvency. This program will have the following general guidelines: ensure the safety of their workers and facilities; reduce corporate and administrative costs; fulfill financial and labor obligation on time; prioritize investment projects according to their profitability; ensure transparency and competition in the procurement process of goods and services; improve productivity and cost efficiency in existing projects and, together with the Ministry of Finance, mechanisms will be implemented to reduce current liabilities and promote a timely payment to suppliers.

According to the information provided by PEMEX's CEO, the adjustment plan to be submitted to the Board of Directors next week, amounts to 100 billion pesos.

In compliance with the provisions of the Federal Budget and Fiscal Responsibility Law, the President, through the Ministry of Finance, will send to Congress a

report on the amount of programmable expenditure to be reduced and the composition of the adjustments. The government will also provide timely information on the development of the preemptive fiscal adjustment in the Reports of Public Finances and in the following link: ww.transparenciapresupuestaria.gob.mx

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