



Monthly perspective | December 8, 2017

## Outlook 2018: looking at the abyss

### SUMMARY

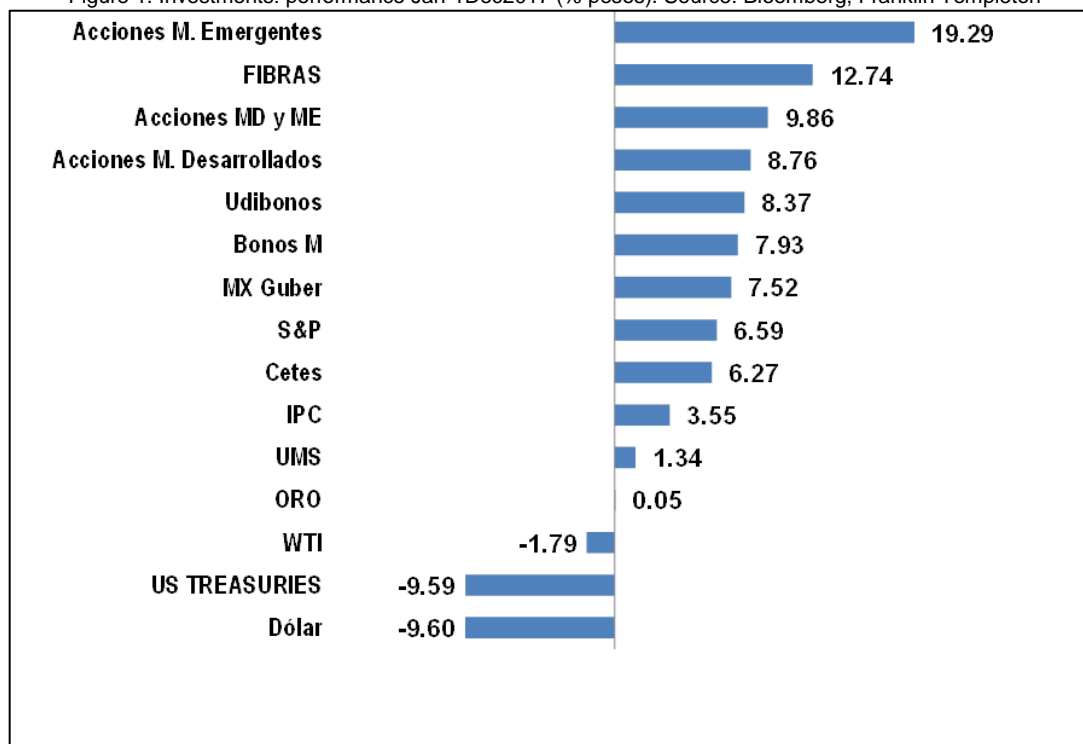
- In 2017, despite political unpredictability in the US, surprises in Europe, and geopolitical risks in Asia and the Middle East, the global economy and risk investments flourished.
- In Mexico, in spite of NAFTA renegotiations and a difficult election outlook for 2018, growth and investments have underperformed globally, but still been positive.
- For 2018, foreseeable global risks are similar: pro-growth initiatives in US, problems in Europe, geopolitical crises, implementation of monetary tightening, and Bitcoin.
- In Mexico, abnormal and extreme risks: NAFTA renegotiation and July 2018 elections.
- Investment scenarios 2018. No change with probabilities: positive (20%), negative (40%), middle (40%).
- Overweight ILS medium term debt, underweight stocks and Fibras.

“When you look at the abyss, the abyss also looks at you”. – Friedrich Nietzsche

### Investments YTD: globally strong, locally weak, but positive

Up to end-November, EM shares, Fibras and DM shares were the best investments in 2017. The worst performing Mexican investments were stocks owing to uncertainty about NAFTA renegotiations and July 2018 elections. In this Perspective, we analyze the political and economic backdrop in 2017 (both global and local) which explains investment performance. We then present our scenarios for 2018, and consequent investment strategy.

Figure 1. Investments: performance Jan-1Dec2017 (% pesos). Source: Bloomberg, Franklin Templeton



**2017: POLITICS AND ECONOMICS****USA**

Before he was inaugurated as President on January 20, Donald Trump had made election promises. In relation to domestic policy: immigration, healthcare, and the economy (deregulation and tax reform). In relation to foreign policy: trade and climate change (see Monthly Perspective – December, 2016).

Figure 2. Trump administration: important events January 20 – December 1, 2017. Source: Franklin Templeton

Date	Event
20-Jan-17	Inauguration
23-Jan-17	Executive order of withdrawal from TPP
26-Jan-17	Executive order for construction of wall on Mexican border. President Peña Nieto cancels trip to Washington
27-Jan-17	American Manufacturing Council set up by Trump
28-Jan-17	Executive order for travel ban on visitors from 7 Muslim countries
30-Jan-17	Executive order eliminating 2 regulations for each new regulation
30-Jan-17	Nomination of Neil Gorsuch to Supreme Court
2-Feb-17	Strategic and Policy Forum holds first meeting
13-Feb-17	Michael Flynn, National Security Advisor, fired
6-Mar-17	Executive order revising travel ban to cover 6 Muslim countries, excluding Iraq
10-Apr-17	Neil Gorsuch confirmed for Supreme Court
9-May-17	James Comey, Director FBI, investigating relations of Trump campaign with Russia, fired
17-May-17	Robert Mueller named Special Counsel to investigate relations of Trump campaign with Russia
1-Jun-17	Trump announces withdrawal of US from Paris Agreement on Climate Change
21-Jul-17	Sean Spicer, White House Press Secretary, resigns
29-Jul-17	John Kelly, ex general US army, appointed White House chief of staff. Reince Priebus resigns.
16-Aug-17	Strategic and Policy Forum and American Manufacturing Council disbanded by Trump
18-Aug-17	Stephen Bannon, White House chief strategist, resigns
26-Sep-17	"Trumpcare", Republican initiative to replace or repeal Obamacare, rejected
30-Sep-17	Tom Price, Secretary for Health and Human Services, resigns
30-Oct-17	Paul Manafort, exhead of Trump campaign, accused by Mueller on charges related to Russia/Trump campaign
2-Nov-17	Jerome Powell, Fed board member, proposed by Trump as replacement for Janet Yellen as Fed President
1-Dec-17	Michael Flynn, exNational Security Advisor, admits lying to FBI in relation to Russia

**Domestic policy***Immigration and healthcare*

On January 28, Trump approved an executive order for a ban for travelers from 7 Muslim countries, which was challenged before the Supreme Court and had to be revised twice before being approved. Restrictions were also introduced on the children of illegal immigrants born in the US (Deferred Action for Childhood Arrivals - DACA), which have not yet been implemented. The initiative to build a wall on the Mexican border against illegal immigration has advanced in terms of bids for construction but has not been implemented. There was an attempt to recall or replace Obamacare but it was rejected by the legislature (Figure 2).

*Deregulation*

The most important measure, also in Trump's first 10 days, was to pass an executive order that required the elimination of two existing regulations for the introduction of each new one. The impact of this measure has been to slow down the introduction of new regulations, to obstruct the implementation of many of the 527 new regulations passed in Obama's last year (2016), or encourage light enforcement, in the environmental, labor, financial, justice and health and safety sectors<sup>1</sup>. Most difficult of all has been the elimination of existing regulations, but in general the focus on deregulation, owing to the diminution of regulatory uncertainty, has helped business confidence.

*Tax reform*

The reduction of corporate and individual taxes has caused controversy, between those who believe that they will pay for themselves as increased growth will lead to increased revenues, and those who believe that it will lead to an increased deficit (more than US\$1trn.). In an open letter to Steven Mnuchin, Treasury Secretary, an important group of economists expressed the opinion that the reform is growth positive<sup>2</sup>. In general they consider that the tax reductions will increase growth and that the confirmation of a progrowth objective increases business confidence. Tax reform would be the first legislative initiative approved in Trump's first year, increasing investor and consumer confidence, which is reflected by the record levels of US stock markets (see page 10).

*Supreme Court and Fed*

Trump named Neil Gorsuch to the Supreme Court, and he was ratified in April. Trump named Jerome Powell to the leadership of the Fed, having been a board member since May 2012, to maintain the continuity of the gradual

<sup>1</sup> Regulation Tracker. Brookings Institution (see <https://www.brookings.edu/RegTracker>)

<sup>2</sup> Wall Street Journal, November 26, 2017

monetary normalization cycle begun by Janet Yellen, and continue a process of moderate financial deregulation. He was ratified by the Senate on December 6, and his period begins in February, 2018.

### Foreign policy

There have been more concrete measures in foreign than domestic policy. On trade, Trump announced withdrawal from the TPP (TransPacific Partnership) on January 23, 3 days after his inauguration (Figure 2). On climate change, Trump announced the US withdrawal from the Paris Treaty in June, 2017. NAFTA renegotiation was announced in May and began in August 2017. After 5 rounds, its termination was postponed from December 2017 to March 2018. During 2017, unexpected foreign policy crises occurred. In Syria, Trump had to face Russian and Iran, who support the current regime. North Korea has tested nuclear missiles, with threats to launch them not only against South Korea, but also Japan and the US, and the US has reached out to China to control its neighbor. In a more dangerous world, some derive solace from the fact that Trump has surrounded himself with 3 ex-generals (James Mattis, Defense Secretary, Ray McMaster, National Security Advisor, and John Kelly, Chief of Staff).

### Governing style

Unpredictability has been the hallmark of Trump's first year, accentuated by incessant use of tweets. It also affects his relationship with subordinates, who are not always in coordination. There have been changes in his close advisory circle: Flynn, Spicer, Priebus, and Bannon have resigned or been fired (Figure 2). Of the cabinet, only Tom Price, Health Secretary, has gone. The future of other cabinet members (e.g. Jeff Sessions, Justice, and Rex Tillerson, State), is also in doubt.

### Russiagate

A constant drumbeat of the Trump administration have been the allegations of contacts with Russia between him, his family and his circle in relation to the 2016 elections. The FBI under James Comey had begun an investigation of "Russiagate". After Comey's dismissal in May, 2017, Robert Mueller was appointed Special Counsel by the Justice Department to continue the investigation, which has been expanded to campaign executives, his family and even to his own business dealings (e.g. recent revelations of Trump dealings with Deutsche Bank). Despite Trump's repeated attempts to block the investigation, various people have admitted to lying about contacts with the Russians during the campaign and are now cooperating with the investigation (e.g. Michael Flynn – Figure 2). The probability of an impeachment motion against Trump, in relation to Russiagate, has increased to 50%<sup>3</sup>.

## OUTSIDE USA

### Elections

Figure 3. Important elections 2017. Source: Franklin Templeton

Date	Country	Election	Winning party	Change (seats)	Leader
15-Mar-17	Holland	Parliament	VVD	-8	Mark Rutte
7-May-17	France	President and parliament	En Marche	NA	Emmanuel Macron
8-Jun-17	UK		Conservador	-13	Theresa May
24-Sep-17	Germany	Parliament	CDU/CSU	-65	Angela Merkel
22-Oct-17	Japan	Parliament	Lib/Dem	-6	Shinzo Abe

In France, Emmanuel Macron, leader of the newly formed En Marche party, won a strong victory against Marine LePen, leader of the Front National extreme right party. In Holland, UK and Germany there was continuity, but the incumbents lost seats to extreme opposition parties (right in Holland and Germany and left in UK), and had to form coalitions to govern.

### Brexit

Theresa May, UK prime minister, began the Brexit process on March 29 2017, to withdraw from the European Union on March 29, 2019. To strengthen her party in the negotiations, May held elections on June 8 2017, but an unfavorable result forced her to maintain a governing majority by forming a coalition with the 10 MPs of the Democratic Unionist Party of Northern Ireland. Brexit negotiations began on June 19, 2017, over three key issues: 1) Rights of UK citizens in EU and vice versa, 2) The cost of the "divorce" and 3) the frontier between Northern Ireland and the Republic of Ireland. In the week beginning December 4, it seemed as if all these elements had been resolved, but, at the close of this report, agreement had not been reached.

<sup>3</sup> The Independent (<http://www.independent.co.uk>), December 4, 2017

## Catalonia

After the referendum vote in favor of Independence on October 1, the Catalan parliament officially declared Independence on October 27. The Spanish Senate approved the application of Article 155, by which the Spanish government officially dissolved the Catalan government and announced regional elections for December 21. The EU backed the Spanish government decision and has confirmed it will not recognize Catalan independence.

## European Central Bank (ECB)

The ECB announced the end of years of monetary stimulus through monthly bond purchases. The value of bonds will fall starting January 2018 from €60bn. to €30bn. monthly, probably until autumn 2018, in sync with the Fed.

## Bitcoin

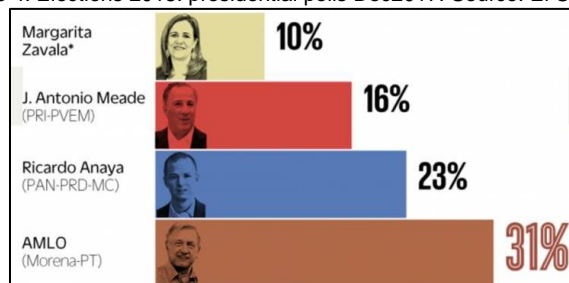
Bitcoin, a peer to peer electronic cash system called “cryptocurrency”, was invented by a pseudonymous person called Satoshi Nakamoto. The uniqueness of the concept is that it is a worldwide payment system, decentralized and digital, without a central repository or single administrator. The network is peer to peer and transactions take place between users through the use of cryptography. Transactions are verified by network codes and recorded in a public ledger called a blockchain. The bitcoin network came into existence on January 1, 2009, when the first ever block was “mined” as part of a blockchain: the process of verifying transactions and ensuring the validity of a blockchain is called “mining”. Since then, an estimated 2,000 or more cryptocurrencies have been created with an estimated market capitalization of more than US\$200 bn.: there are an estimated 129 focused hedge funds and 121 cryptocurrency exchanges globally<sup>4</sup>. The global supply of bitcoins is capped at 21 mn and currently estimated at 16 mn. Its supporters claim that it is a free market phenomenon, unconstrained by monopoly central banks, and therefore more reliable. Its detractors consider it a mechanism for money laundering, and that its value simply reflects demand for money laundering. While a bitcoin was priced around US\$0.3 in 2011, its price is now above US\$16,000. Owing to the classic boom features of price rise, volatility, and impossibility to understand the fundamentals underlying its value, many consider Bitcoin, and other cryptocurrencies, ready for a crash, with incalculable consequences for investors, financial markets, and, possibly, the real economy.

## MEXICO

### Elections 2018

By December 2017, the electoral landscape had become clearer, with virtual candidates now nominated for both the PRI (José Antonio Meade - JAM) and Morena (Andrés Manuel López Obrador – AMLO). On December 6, Aurelio nuño, Minister of Education, resigned to become Meade’s campaign manager. The candidate for the coalition Citizens’ Front (Frente Ciudadano) between right PAN and center left PRD had still to be determined between Ricardo Anaya (PAN) and Miguel Angel Mancera (PRD). Leading independent candidates were: Jaime Rodriguez (“El Bronco”), still Nuevo León governor, and Margarita Zavala (wife of former President Felipe Calderón.). With PRI and Morena the most organized, coherent parties, it seems currently that the fight between the two will depend on their ability to peel voters from the incoherent Frente, or independents. While AMLO appears to have moderated his message and approach to government, voters remember his prior campaigns (2006 and 2012), when he threatened to destroy institutions, and showed messianic tendencies. For many, the issue is whether he will turn out like Luiz Inácio Lula da Silva (Lula - Brazilian President 2003-2011), who turned moderate, or Hugo Chavez (Venezuelan President 1999-2011), who destroyed his country. These are the concerns that affect the markets, and are likely to do so until the July 2018 elections. While AMLO currently has a clear lead (Figure 4), voters remember that he was in a similar situation at a similar stage in a prior election (2006), only to lose to Felipe Calderón.

Figure 4. Elections 2018: presidential polls Dec2017. Source: El Universal



<sup>4</sup> <https://cryptocoincharts.info/markets/info>

## NAFTA negotiations

Figure 5. NAFTA renegotiation: timeline. Source: IIF

Date	Event
Jan-18	6th negotiation round
Feb-18	7th negotiation round
Feb-May 18	90-day notification of intention to sign
Mar-18	Mexico presidential campaign starts
1-Jul-18	Mexico presidential elections
Jul-18	Trade promotion authority expires
6-Nov-18	US midterm elections
1-Dec-18	Mexico president takes office

Since the initial notification of NAFTA renegotiation in May, there were 5 rounds. After 6 days of the 5th round, it was announced that the process would be stretched from end-2017 until the end of the first quarter of 2018 (Figure 5). The main issues are the auto sector, rules of origin, dispute resolution and a “sunset” clause, whereby NAFTA would cease to exist each 5 years unless the three countries decided to renew it. If NAFTA were eliminated, the three countries would have recourse to the rules of the World Trade Organization (WTO) and most favored nation (MFN) clause. Mexican exports to the US would have an average tariff of 3.5%, and US exports to Mexico of 7.0%. 42% of Mexican exports to the US do not use NAFTA tariffs, but MFN. Even so, an unfavorable outcome of the renegotiation could reduce confidence in the economy and Investment, and strengthen parties of the left for the July elections, with a negative effect on peso investments.

### Mexican Treasury (SHCP) and Bank of Mexico (Banxico)

At the end of November, Treasury Minister José Antonio Meade resigned to become PRI “precandidate” for the 2018 presidential election. President Peña Nieto appointed José Antonio González Anaya, Director General de Pemex, in Meade’s place, appointing Carlos Treviño to replace González Anaya in Pemex. Alejandro Díaz de León, deputy governor of Banxico, was appointed governor of the central bank, in place of Dr. Agustín Carstens, who took up his post as Managing Director of the BIS in Basel on December 1, 2017.

## 2018: OUTLOOK

### POLITICAL CALENDAR

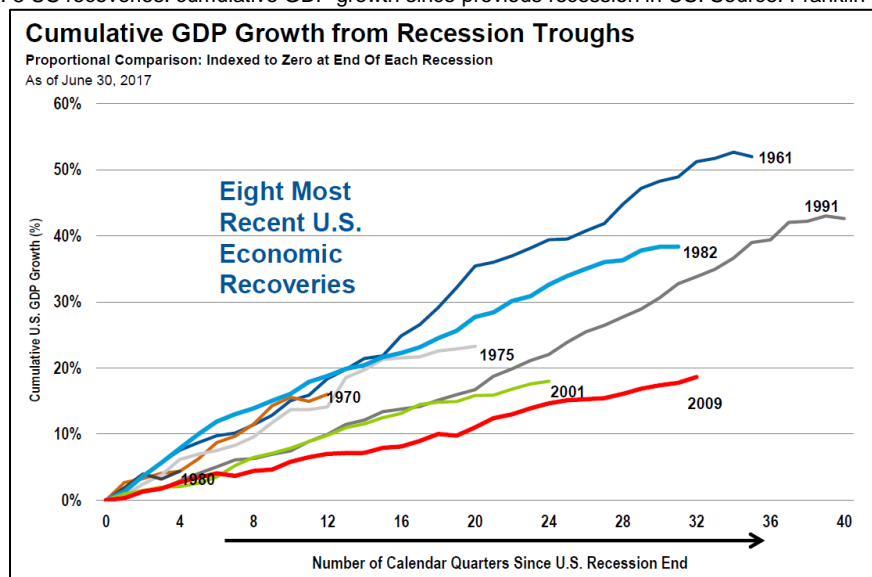
Main elections in 2018 include Latin America (Colombia, Mexico, Brazil and Venezuela), Europe (Czech Republic, Russia, Italy, Sweden), and the US (Figure 6).

Figure 6. Main elections 2018. Source: Franklin Templeton

Date	Country	Election
13-Jan-18	Czech Republic	President
18-Mar-18	Russia	President
20-May-18	Italy*	Parliament
27-May-18	Colombia	President
1-Jul-18	Mexico	President and Congress
9-Sep-18	Sweden	Parliament
7-Oct-18	Brazil	President and Congress
17-Oct-18	Venezuela	President
6-Nov-18	USA	Senate and Congress
* Elections before May 20		

## ECONOMY US

Figure 7. 8 US recoveries: cumulative GDP growth since previous recession in US. Source: Franklin Templeton



The current US recovery is close to 20% GDP growth, 8 years after the last recession at end 2009. It will be the third longest recovery, and slowest of the last 8 in the US, owing to the severity of the 2008 financial crash (Figure 7).

## GLOBAL

Figure 8. Developed and emerging economies: estimated GDP growth (%) 2017 y 2018 (oct2017) Source: IMF

	2016	Projections	
		2017	2018
<b>World Output</b>	<b>3.2</b>	<b>3.6</b>	<b>3.7</b>
<b>Advanced Economies</b>	<b>1.7</b>	<b>2.2</b>	<b>2.0</b>
United States	1.5	2.2	2.3
Euro Area	1.8	2.1	1.9
Germany	1.9	2.0	1.8
France	1.2	1.6	1.8
Italy	0.9	1.5	1.1
Spain	3.2	3.1	2.5
Japan <sup>2</sup>	1.0	1.5	0.7
United Kingdom	1.8	1.7	1.5
Canada	1.5	3.0	2.1
Other Advanced Economies <sup>3</sup>	2.2	2.6	2.5
<b>Emerging Market and Developing Economies</b>	<b>4.3</b>	<b>4.6</b>	<b>4.9</b>
Commonwealth of Independent States	0.4	2.1	2.1
Russia	-0.2	1.8	1.6
Excluding Russia	1.9	2.9	3.3
Emerging and Developing Asia	6.4	6.5	6.5
China	6.7	6.8	6.5
India <sup>4</sup>	7.1	6.7	7.4
ASEAN-5 <sup>5</sup>	4.9	5.2	5.2
Emerging and Developing Europe	3.1	4.5	3.5
Latin America and the Caribbean	-0.9	1.2	1.9
Brazil	-3.6	0.7	1.5
Mexico	2.3	2.1	1.9
Middle East, North Africa, Afghanistan, and Pakistan	5.0	2.6	3.5
Saudi Arabia	1.7	0.1	1.1
Sub-Saharan Africa	1.4	2.6	3.4
Nigeria	-1.6	0.8	1.9
South Africa	0.3	0.7	1.1
<b>Memorandum</b>			
European Union	2.0	2.3	2.1
Low-Income Developing Countries	3.6	4.6	5.2
Middle East and North Africa	5.1	2.2	3.2
World Growth Based on Market Exchange Rates	2.5	3.0	3.1



International Monetary Fund (IMF) forecasts that growth in the US will continue (2.2% in 2017 to 2.3% in 2018), but not in the Eurozone (2.1% a 1.9% - Figure 8). However, growth will continue in emerging economies (4.6 a 4.9%), with important advances in the poorest countries (e.g. Middle East and North Africa 2.2% to 3.2%). These estimates are reflected in the Bloomberg consensus of private economists (Figure 9).

Figure 9. Developed and emerging economies: estimated growth 2017 and 2018 (dic2017) Source: Bloomberg

Developed				Emerging			
Growth(%)				Growth(%)			
	2018 E	2017 E	2016		2018 E	2017 E	2016
World	3.61	3.50	2.90	World	3.61	3.50	2.90
Developed	2.20	2.24	1.68	Emerging	4.92	4.51	3.74
US	2.48	2.20	1.60	China	6.45	6.80	6.70
Euro Area	1.90	2.20	1.70	India	6.70	7.10	7.50
Japan	1.20	1.50	1.00	Rusia	1.85	1.80	(0.50)
Britain	1.40	1.50	2.00	Brasil	2.50	0.70	(3.50)
Australia	2.75	2.30	2.40	México	2.22	2.10	2.10
Canada	2.20	2.20	1.30	Corea del sur	2.90	5.10	2.70
Germany	1.80	2.20	1.85	Indonesia	3.65	5.10	5.00
France	1.80	1.80	1.10	Turquia	3.65	5.30	2.20

## MEXICO

For Mexico, domestic growth estimates are similar to foreign ones (Figure 10). Inflation is expected to fall, due to removal of the effect of the gasoline price hike (in January 2017), in January 2018 (Figure 11).

Figure 10. Mexico: GDP growth estimates (%)

	2017	2018
SHCP	2.0 - 2.6	2.0 - 3.0
Banxico	1.8 - 2.3	2.0 - 3.0
Encuesta Banxico (Diciembre 2017)	2.10	2.30
Fondo Monetario Internacional (Octubre 2017)	2.10	1.90
Banco Mundial (Junio 2017)	1.80	2.20
Bloomberg (Diciembre 2017)	2.10	2.20
IMEF (Noviembre 2017)	2.10	2.30
Promedio	2.10	2.30

Figure 11. Mexico: inflation estimates (%)

	2017	2018
SHCP	5.80	3.00
Encuesta Banxico (Diciembre 2017)	6.50	3.84
Fondo Monetario Internacional (Octubre 2017)	6.05	3.48
Bloomberg (Diciembre 2017)	6.00	3.90
IMEF (Noviembre 2017)	6.30	3.80
Promedio	6.13	3.60

## 2018: SCENARIOS

### Risks

In relation to the political and economic risks in 2017, foreseeable risks for the 2018 scenarios are similar, with the exception of the emergence of Bitcoin:

#### Global

- US: Trump progrowth policies (taxes, deregulation, infrastructure)
- North America: NAFTA renegotiation
- Europe: Brexit, Catalonia and elections
- Geopolitics: Middle East, Russia, China, North Korea
- Global slowdown: reduction of monetary easing by central banks
- Bitcoin

#### Local

- 2018 presidential and congressional elections
- Post-earthquake reconstruction
- Security
- Corruption
- Oil price
- Debt increase: credit rating

## Scenarios

Taking account of the foreseeable risks outlined in the previous section, we present three scenarios for 2018, where the objective is economic growth in Mexico. In the positive case, all risks turn out favorable for Mexican growth, in the negative case, unfavorable, and in the middle case, there is a mix of risks (by nature, intensity and duration).

### Positive (20%)

In the US, an effective combination of tax reduction, deregulation and infrastructure measures is implemented, increasing growth. NAFTA is successfully renegotiated. Risks in Europe, China, Russia, Korea and the Middle East do not materialize. Synchronized global growth continues and central banks reduce monetary stimulus successfully. A Bitcoin crash does not occur, or it occurs without materially affecting the broader economy. In Mexico, security and corruptions risks are contained. The July election outlook is positive, as are its results.

### Negative (40%)

In the US, progrowth measures fail, as does NAFTA renegotiation. The UK and the EU collapse, and risks in Europe, China, Russia, North Korea and the Middle East materialize. There is a global slowdown caused by political factors, economic dynamics, or central Banks. There is a Bitcoin crash, which affects the broader economy in unexpected ways. In Mexico, security and corruption problems increase, the outlook for July elections deteriorates, and its results make the political climate even worse.

### Middle (40%)

In the US, progrowth measures are implemented partially and NAFTA is renegotiated with mixed results. Some risks in Europe, China, Russia, Korea and the Middle East materialize partially. Global growth continues but less synchronized than in and central banks are not always efficient, efficacious and effective. A Bitcoin collapse affects investor confidence. In Mexico security and corruption problems are partially contained. The outlook for July elections is uncertain, and its results only partially positive.

## MARKETS

### US\$ and peso

The US\$ weakened against other currencies (Figure 12). Owing to a slight improvement in NAFTA prospects, peso undervaluation fell from -27% to -25% (Figure 13).

Figure 12. US\$ index and peso 2004-Dec2017. Source: Bloomberg

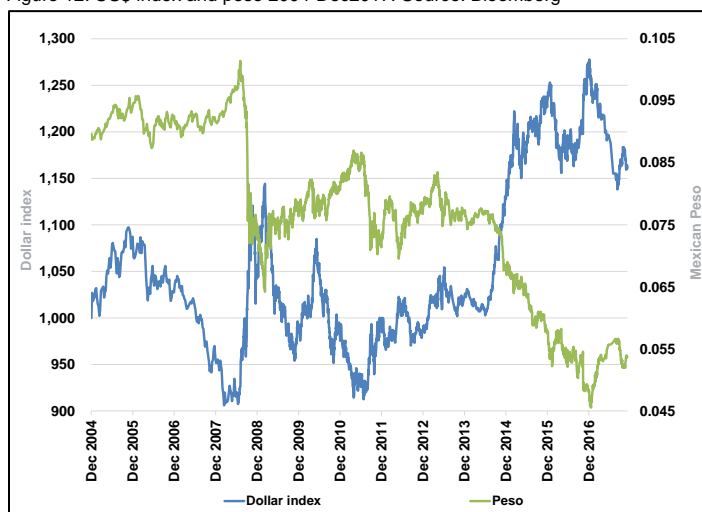
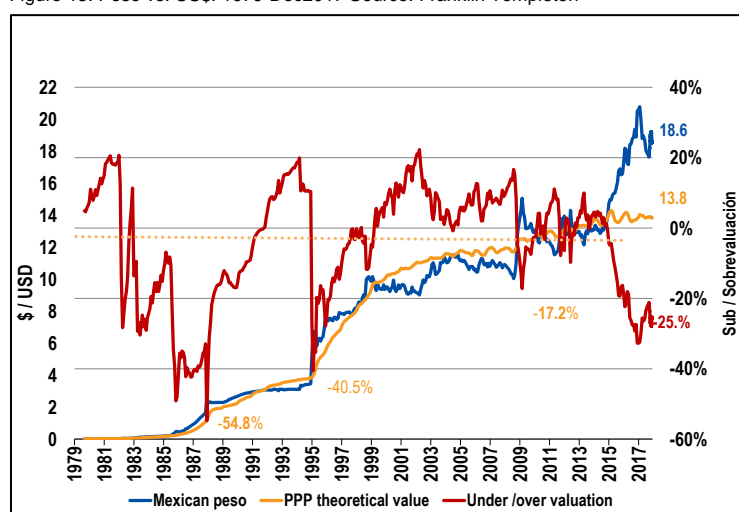


Figure 13. Peso vs. US\$: 1979-Dec2017 Source: Franklin Templeton

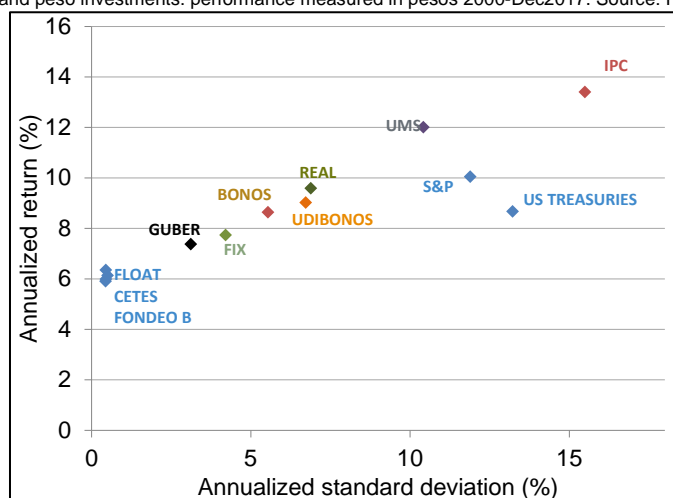


### Comparative long term performance of US\$ and peso investments

Despite peso depreciation, long term (2000-2017), peso denominated investments have outperformed US\$ denominated investments, measured in pesos (Figure 14).



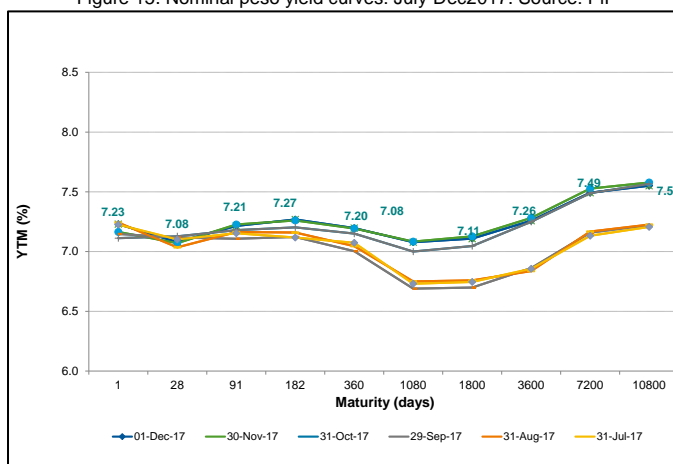
Figure 14. US\$ and peso investments: performance measured in pesos 2000-Dec2017. Source: Franklin Templeton



## Debt

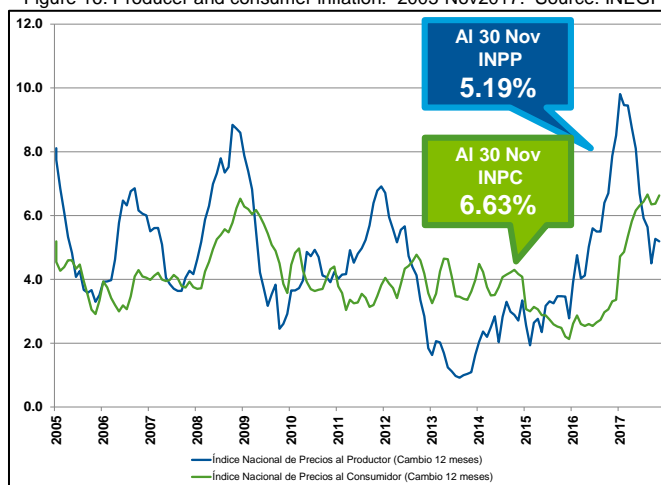
During October and November, the nominal yield curve rose over all terms, leading to a greater normalization of the curve (Figure 15).

Figure 15. Nominal peso yield curves: July-Dec2017. Source: PiP



In October and November, consumer price inflation rose slightly to 6.63% (6.37% previous - Figure 16). For 2018, inflation is expected to fall, owing to removal of the gasoline price hike that occurred in January 2017 from the 2018 inflation calculation.

Figure 16. Producer and consumer inflation: 2005-Nov2017. Source: INEGI



By end 2018, according to the Bloomberg consensus, 10 year rates will rise in all developed economies, but will fall in emerging economies, except China, South Korea, and Indonesia (Figure 17).

Figure 17. Developed and emerging economies: 10 year bond yields forecast for end-2018 (Dec2017). Source: Bloomberg, Franklin Templeton

Developed				Emerging			
local 10y yields (%)				local 10y yields (%)			
	4Q18e	Actual	Aumento (bps)		4Q18e	Actual	Aumento (bps)
US	2.85	2.38	47	China	3.97	3.93	4
Euro Area	0.93	0.33	60	India	6.75	7.08	(33)
Japan	0.12	0.04	9	Rusia	7.17	7.39	(22)
Britain	1.67	1.29	38	Brasil	8.10	10.34	(224)
Australia	3.14	2.54	60	México	7.25	7.27	(2)
Canada	2.69	1.93	76	Corea del sur	2.74	2.48	26
Germany	0.93	0.33	60	Indonesia	7.05	6.54	52
France	1.15	0.64	51	Turquia	10.79	12.08	(129)

## Stocks

Figure 18. Earnings per share (EPS) growth for MSCI AC World Index 1988-2017

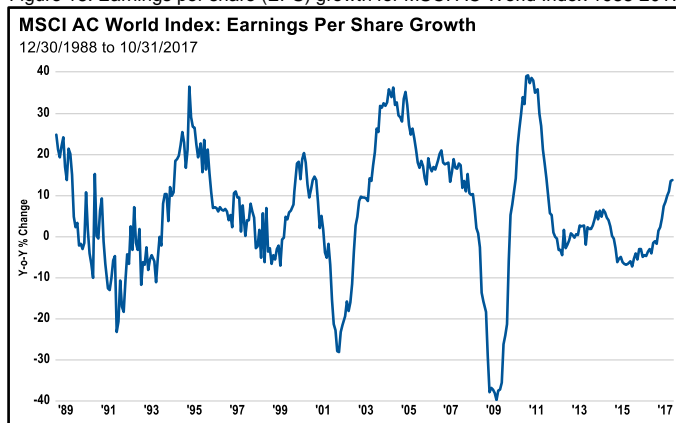
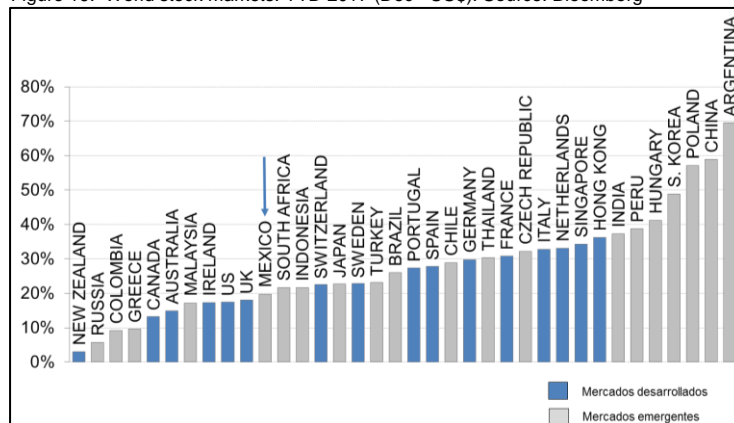
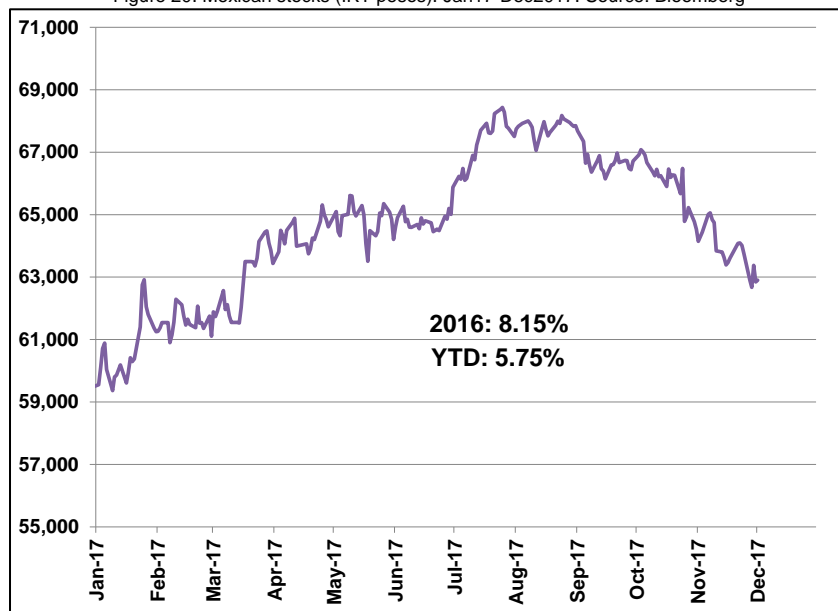


Figure 19. World stock markets: YTD 2017 (Dec - US\$). Source: Bloomberg



Global stock markets have been driven upward by the increase in EPS (Figure 18). Mexican stock performance in US\$ and pesos was affected by uncertainty over NAFTA renegotiation and 2018 elections (Figures 19 and 20).

Figure 20. Mexican stocks (IRT pesos). Jan17-Dec2017. Source: Bloomberg



## Fibras

Owing to novelty, high dividends, and inflation protection, Fibras (Mexican REITs), have outperformed stocks from 2011 to 2017 (Figure 21). Fibras will reflect uncertainty over NAFTA renegotiation, and, depending on NAFTA developments, could remain attractive (Figure 22).

Figure 21. Fibras vs. Mexican stocks (IRT) Mar2011-Dec2017 (base 100 MXN\$). Source: Bloomberg

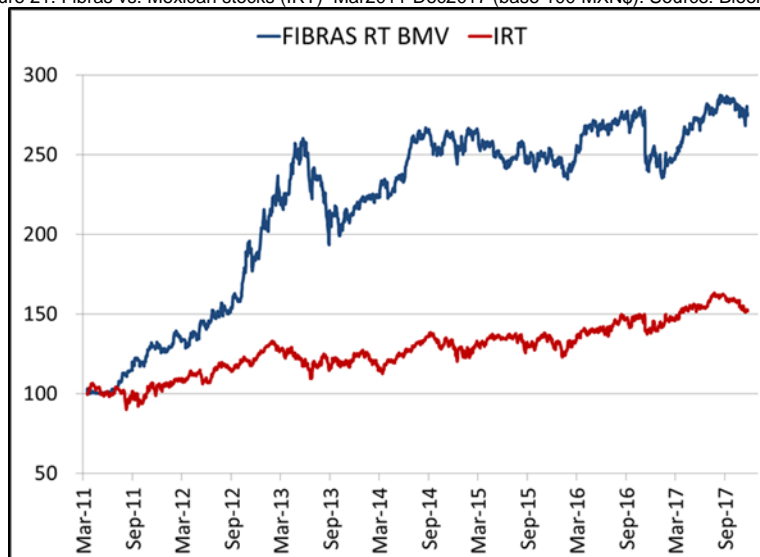


Figure 22. Fibras: valuation and dividends (Dec2017). Source: Franklin Templeton

	Mcap (M) (MXN)	Calendarized						
		2013	2014	2015	2016	2017	2018	2019
FUNO11 MM	110,529	4.2%	6.2%	6.8%	6.7%	6.9%	7.4%	8.3%
DANHOS13 MM	44,986	1.2%	5.6%	6.2%	6.7%	6.6%	6.9%	7.5%
TERRA13 MM	23,264	4.0%	6.6%	6.6%	7.1%	8.6%	8.7%	8.8%
FIBRAPL MM	23,178		2.5%	4.5%	5.6%	6.0%	6.5%	6.9%
FIBRAMQ MM	17,631	8.9%	7.6%	7.0%	8.6%	7.0%	7.7%	8.4%
FIHO12	10,074	6.3%	7.2%	7.1%	7.8%	7.5%	9.2%	11.2%
FHIPO	8,972			10.5%	10.6%	10.9%	11.6%	13.3%
FMTY14 MM	8,007				7.6%			
FSHOP13 MM	5,294		8.1%	9.1%	9.8%	8.6%	7.2%	7.2%
FINN13 MM	5,179	5.8%	6.7%	6.2%	7.6%	8.5%	9.0%	9.8%

## Conclusion

While the global Investment outlook continues favorable, Mexico is subject to two abnormal, extreme risks: an unfavorable NAFTA renegotiation, and negative election results in 2018. Until these risks have been reduced or removed, we expect high volatility in Mexican investments: peso, debt, stocks, and fibras. We recommend overweight in ILS medium term debt, and underweight in shares and fibras.

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 December 8, 2017

**Main financial indicators: monthly and YTD performance at November 30, 2017**

In Mexico, the IPC fell 3.15%. Nominal rates rose for the medium and long terms. Real rates rose for 10y. The US\$ weakened 2.74% against the peso. In the US the DJ, S&P500 and Nasdaq rose. Nominal and real rates fell for 30y bonds. In the Banxico survey, optimism rose to 23% (13% previous), no change fell to 47% (50%), and pessimism fell to 30% (38%).

Mexico					
Stock market and oil					
	30-Nov-17	31-Oct-17	Month	YTD 2017	2016
IPC	47,092.44	48,625.53	-3.15%	3.18%	6.20%
Local currency (USD/MXN)	18.62	19.15	-2.74%	-9.68%	19.53%
Mexican oil mix (USD/bl)	53.59	52.72	1.65%	15.75%	69.16%
Nominal rates					
	30-Nov-17	31-Oct-17	Month	YTD 2017	2016
CETES 28	7.07%	7.13%	-6 bps	123 bps	279 bps
CETES 360	7.19%	7.15%	4 bps	76 bps	277 bps
M5	7.13%	7.05%	8 bps	-8 bps	166 bps
M10	7.28%	7.25%	3 bps	-22 bps	118 bps
M30	7.58%	7.57%	1 bps	-24 bps	87 bps
Real rates					
	30-Nov-17	31-Oct-17	Month	YTD 2017	2016
UDIBONO 10	3.39%	3.36%	3 bps	34 bps	-29 bps
UDIBONO 30	3.70%	3.72%	-2 bps	-9 bps	-12 bps
Commodities					
	30-Nov-17	31-Oct-17	Month	YTD 2017	2016
Gold	1,275.01	1,271.45	0.28%	10.08%	9.15%
WTI (USD/bl)	57.4	54.38	5.55%	6.85%	41.97%
UMS					
	30-Nov-17	31-Oct-17	Month	YTD 2017	2016
UMS 10 years	3.58%	3.64%	-6 bps	-69 bps	40 bps
UMS 20 years	4.47%	4.57%	-10 bps	-80 bps	-3 bps
UMS 30 years	4.59%	4.70%	-11 bps	-67 bps	-3 bps
Stock markets (US\$)					
	30-Nov-17	31-Oct-17	Month	YTD 2017	2016
MSCI Developed	8,350.80	8,169.60	2.22%	21.39%	8.15%
MSCI Emerging	2,433.14	2,428.13	0.21%	32.91%	11.60%
MSCI Mexico	9,404.59	9,448.62	-0.47%	16.33%	-8.98%
MSCI Brazil	6,050.35	6,243.94	-3.10%	18.89%	66.75%

US					
Stock market					
	30-Nov-17	31-Oct-17	Month	YTD 2017	2016
DJ	24,272.35	23,377.24	3.83%	22.82%	13.42%
S&P	2,647.58	2,575.20	2.81%	18.26%	9.54%
Nasdaq	6,873.97	6,727.67	2.17%	27.69%	7.50%
Nominal rates					
	30-Nov-17	31-Oct-17	Month	YTD 2017	2016
Tbill 90	1.27%	1.15%	12 bps	76 bps	35 bps
Tnote 5	2.14%	2.01%	13 bps	21 bps	17 bps
Tnote 10	2.42%	2.38%	4 bps	-3 bps	18 bps
Tbond 30	2.83%	2.88%	-5 bps	-23 bps	5 bps
Real rates					
	30-Nov-17	31-Oct-17	Month	YTD 2017	2016
Tip 5	0.41%	0.22%	19 bps	32 bps	-36 bps
Tip 10	0.56%	0.50%	6 bps	6 bps	-23 bps
Tip 30	0.88%	0.92%	-4 bps	-11 bps	-29 bps

Bank of Mexico survey		
Indicator	2017	2017 anterior
PIB	2.28%	2.25%
Inflation	3.91%	3.85%
Cetes 28	6.73%	6.72%
Local currency	18.79	18.61
Business conditions		
	30-Nov-17	31-Oct-17
Optimism	23%	13%
No change	47%	50%
Pessimism	30%	38%

Source: Bloomberg, Banco de México

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\*Timothy Heyman, President of FTSAM, founded Heyman y Asociados in 1985. In 2013, Franklin Templeton established FTSAM and merged it with Heyman y Asociados.

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