



Mexico Fights Back

7 July 2017

By **Thomas Hughes**
Senior Editor of Global
Investor Spotlight



Mexican stocks have been in rally mode as Trump backs down from scrapping NAFTA.

The Tables Have Turned

Even as President Donald Trump backs down on calls to scrap NAFTA Mexican officials send him a warning. The message, there are opportunities and avenues for Mexican businesses

with or without the US. The latest round of political rhetoric began a few weeks ago when President Trump announced NAFTA could stay in place “at this time”. His message was surprising in that it came only hours after “sources” revealed a draft Executive Order withdrawing the US from NAFTA was in existence.

The reason for the about face is simple to see if not understand. The President had spoken to both President Peña Nieto of Mexico and President Trudeau of Canada in attempts at paving the way for a smooth renegotiation of the agreement. All three parties have agreed to do so as swiftly as possible

within their respective governmental systems with an expected start date sometime this summer.

Even so, Mexican Minister of Economy Ildefonso Guajardo Villarreal, has sent a message to President Trump to the effect Mexico has alternatives to the US and is pursuing them. His comments pertained to a planned September visit by Mexican officials to China whose purpose is further exploration of renewed trade ties with China. Mexico and China have had positive trade ties in the past but they’ve cooled since a 2015 incident involving a Chinese rail builder.

Minister Guajardo “We will use

◀ (the visit) geopolitically as strategic leverage" . . . "It sends the signal that we have many alternatives." The two countries began to move closer last year when Chinese officials visited Latin America. The biggest issue the two face is that in terms of manufacturing they are more often than not competitors. Guajardo further notes that Mexico has had some success persuading China to ease trade barriers and open up new areas for trade.

China is not Mexico's only alternative. The country is in process of improving ties with other Latin American nations, namely Argentina and Brazil, in an effort to increase trade south of their border and provide leverage for negotiations with the US.

Despite Minister Guajardo's efforts, the Mexican economy is still largely dependent on US relations. The most recent data shows the US/Mexico trade deficit grew to \$7 billion in May 2017, a 10 year high as weak peso and strong dollar made cheaper to buy Mexican products. Nearly 80% of Mexican exports go north and that number has been strengthening in recent years. For many companies, this means importing components and finished goods that may otherwise have been manufactured in the US.

Mexican Economy Shines Bright

The Mexican economy has been on a tear for years, since the end of the Global Financial Crisis, and growing at a rate superior to the rest of the world and the US. The country grew at an annualized rate of 2.8% in the first quarter, beating expectations. Along with this, Mexican corporate sales and cash flows for the quarter grew by 18% and 19%, respectively,



as increasing exports and sales abroad had a positive effect when translated to local currency along with strong domestic consumption.

Since the election of Donald Trump, the peso has bottomed from its long-term devaluation and Mexican stocks have been in rally mode. The Mexican Bolsa IPC index has risen nearly 30% in U.S. dollar terms since January 19th, and the peso has risen close to 21% since hitting its low in January.

Managers at The Mexico Fund, Inc see increasing opportunity in Mexican stocks with a focus on the consumer, infrastructure, materials and financials. Top ten holdings include Wal-Mart de México (the nation's largest retailer), Cemex (the

world's largest supplier of white concrete), Fomento Económico Mexicano (global soft-drink supplier, and market leader in convenience stores) and Mexico's top banks. The fund trades on the NYSE under the symbol MXF and pays a quarterly fix distribution of \$0.13 per share.

MXF's NAV has risen 30% since January 19th, when Donald Trump took office. The discount to NAV had been holding steady in the range of 11% to 12% in that time, but has begun to narrow as investor sentiment catches up with the reality of Mexican markets. Looking forward, the Mexican economy can be expected to continue growing and the value of Mexican stocks along with it.

Disclaimer: The opinions in this article are for informational purposes only and should not be construed as a recommendation to buy or sell the stocks mentioned. Please do your own due diligence before making any investment decision.