



## Investment Strategy

# Is the Brussels agreement a definitive solution to the region's debt problems?

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The Brussels agreement isn't just a new bailout package for Greece. It gives form to the European Financial Stability Facility as a kind of financial agency to tackle the European sovereign debt crisis more efficiently. Will its size and the mechanisms designed for its operation be enough to solve the crisis?

On July 20, in a meeting between the leaders of the governments of the 17 euro member countries, agreements and measures were announced for a new rescue package for Greece and to stop the contagion already visible in the over-indebted countries of the region. The survival of the euro was also in question.

The European debt crisis proves that there is no point in having an economic community where member countries have a common parliament, they agree on the free movement of goods, capital and people, where the countries renounce their own currencies for a common currency and a central bank if there is no cross national organization that controls government spending.

Europeans assumed that by putting the fulfillment of a 3% deficit against GDP as a requisite to enter the eurozone, governments were going to act responsibly when

managing their budgets. The large majority of countries reached this level of deficit, and once a member of the euro, forgot about their responsibility in the management of public finances, spending more in order to stay in power and opening the doors to excessive financing.

The euro is so badly planned that it doesn't even contemplate a mechanism for resolving the case of a country that has its debt payment deadlines accumulated over time. Neither does it contemplate until now, what to do with a country that maintains a high fiscal deficit and goes into excessive debt. How should it be sanctioned or how should it be expelled?

On the other side of the coin, financial institutions protected by the high credit ratings of euro member countries, acted irresponsibly by handing out financing in stratospheric volumes. Who is more responsible: the financial institution that gave the financing, the investment fund that bought the government bonds with a good credit rating, or the credit rating agencies?

Once the debt issuer, whether a company or a government, shows it is in a situation of crisis in the financial markets, the credit rating agencies react, always late, lowering the rating. Thus reducing the potential market of the debt.

The European Central Bank did not have the power to buy government bonds on the secondary market. That is the same as the Bank of Mexico not being able to buy cetes (Mexican treasury bonds) on the debt market.

## USA: Congressional Leaders Approve Debt-Limit Increase.

President Barack Obama said at 31th July night that leaders of both parties in the U.S. House and Senate had approved an agreement to raise the nation's debt ceiling by \$2.1 trillion and cut the federal deficit by as much as \$2.5 trillion over a decade, a deal that must now be sold to Congress.

Congressional leaders reached a bipartisan agreement to raise the debt ceiling by at least \$2.1 trillion, sufficient to serve the nation's needs into 2013. They are preparing to sell to members the deal to cut \$917 billion in spending over a decade, raising the debt limit initially by \$900 billion, and to charge a special committee with finding another \$1.5 trillion in deficit savings by the year's end. They confront an Aug. 2 deadline for approval of the agreement. The White House agreed to forgo an automatic tax increase as one of the consequences to kick in if no debt-reduction law is enacted by Christmas.

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## Is Mexico still a good option for investment?

Despite the adverse global economic climate and, above all, the problems of debt in Europe and the United States where interest rates will have to be kept at low levels for some time to come, Mexico is shaping up to be an attractive option for investment due to stability in its macroeconomic variables.

The country has maintained a successful monetary policy by lowering its levels of inflation to under 4.0%, with the potential of ending the year under 3.5%. Banxico will probably maintain its referential rate (currently at 4.5); the peso has been strong throughout the year; and the exchange rate is still under 12 pesos/dollar,

after having reached levels of 15.40 during the recent recession. The country's international reserves are over US\$131 billion while public debt is below US\$57 billion.

Mexico is one of the most open economies and the financial market has maintained a constant flow of foreign investment in Mexican debt instruments, bringing about an increase of MXN245 billion over the year. Income from oil exports was almost US\$20 billion from January to May. The country is expected to receive more than US\$23 billion through remittances.

Meanwhile the economy keeps showing positive signs of recovery with growth over 4.0% this year. Even with the slowdown in the United States, exports are still generating annual rates above 20.0% while consumption, although slow, has maintained an average rate of growth above 3.0% over the last year.

With the presidential elections in our country in 2012, we expect greater government spending to support the economy. Although the insecurity has reduced the GDP, economic growth will probably be maintained over 4.0% for the next two years.

The main risk is Mexico's high level of dependence on the US economy, but we expect acceleration during the second half of the year and the problems with the deficit, although difficult to resolve, will have gradual solutions.

Taking all this into consideration, we still like Mexico as one of the most attractive countries for investment. For the stock market, we are maintaining our estimate of ending the year between 41,500 and 42,000 points which will give a return of around 16.0% at current levels. Companies listed on the stock exchange are, on the whole, reporting good results for the first half of 2011.

## Corporate News

**Alfa completes acquisition of the remaining 49% of Alestra.** Grupo Alfa (ALFA) has completed the acquisition of the 49% of Alestra which was owned by AT&T, with which the Mexican conglomerate now owns 100% of the Mexican telecommunications company. ALFA stated in a press release that the Mexican regulatory authorities had approved the transaction between ALFA and the US telecommunications company. The value of the transaction has not been revealed by any of the companies.

The actions taken by the eurozone governments to tackle the problems in the countries around its periphery have been weak and fallen short. The problems of accumulated payment deadlines of a country such as Greece, which represents less than 3% of the GDP of the eurozone, have managed to put in check the euro system, affecting the entire economy.

Greece owes the equivalent of 143% of its economy and urgently requires the release of an installment of the bailout package agreed in May 2010 to the tune of €110 billion euros, but which was conditioned on reaching certain goals in the reduction of the deficit which are impossible to fulfill when in recession and without being able to make an adjustment in their economy through the devaluation of the currency.

But it also needed another €90 billion to be able to cover its payment deadlines until 2014. The governments called for a new plan to reduce the deficit and an ambitious program of privatization (for an estimated value of €50 billion). Last June, the Greek parliament approved, with great difficulty and huge street demonstrations, all the demands of the Community.

In the Brussels summit in July, a second rescue package was announced for a total of €159 billion, €109 billion of which will be provided by the European governments and the IMF. Financial institutions will contribute €50 billion after agreeing to a series of bond swaps and repurchases that will reduce Greece's debt load.

It is likely that the program of bond exchanges will adopt a scheme similar to the Brady Bonds successfully used for the restructuring of debt in Latin America. With the added security of 30 year zero coupon bonds issued by strong euro members or by the European Financial Stability Facility which will be bundled with the bonds of the issuer (Greece) as a guarantee of capital, the interest rates will be significantly reduced and the term lengthened. But even through these transactions have been proposed as voluntary, the rating agencies may consider it a selective default. The considerable discount that Greek bonds currently carry, means they will obtain a reduction or discount on their debt through the exchange.

But as well as the announcement about the Greek bailout package, the change in focus given to the European Financial Stability Facility created last year was highly significant. Without increasing the value of the fund,

currently €440 billion, the governments have given it powers to buy sovereign bonds in the financial markets. This function was being carried out to a lesser capacity by the central bank until last April when it dropped the function saying it was the job of the governments.

The fund is acquiring the characteristics of a financial agency of the governments, a kind of European monetary fund, now able to issue bonds or grant credit directly to governments to resolve problems of liquidity and capitalize commercial banks in problems. In this way, the European authorities are equipping themselves to face the potential crises in Portugal and Ireland. But the current size of the facility would struggle to support simultaneous crises in Spain and Italy.

Now we need to see if the governments receive approval from their respective parliaments for the proposed modifications to the Stability Facility and when carrying out the swaps, if the markets agree with vote of confidence to reduce the deficits that the countries have got themselves into. But at the bottom of it all, Europe knows that it has to move towards stronger political integration through the creation of a shared Ministry of Finance and the institution of a solid framework of rules and sanctions, including the mechanisms for expelling countries that don't comply with the minimum requirements of fiscal discipline.

What can we expect in the financial markets?

Together with the problem of the US debt ceiling, the Greek problem generated a negative reaction in financial markets faced with uncertainty in which we saw the euro fall to USD1,40 to the €, stock markets fall, treasury interest rates fall, and the rise in prices of raw materials and gold in particular. Following the agreements, there has been a rise in the euro, a slight rise in treasury interest rates, a rising trend in stock markets and a slight fall in the price of raw materials.

There has been a strong reaction in Europe, but a limited reaction on the American continent as there is still no definitive solution to the debt problem in the United States and the reduction of the deficit. We think that 'The Gang six' reform proposal is gaining acceptance among US Congress which could mean it will become the hybrid solution between the Republican and Democrat proposals, allowing the debt ceiling to be raised. We think that once this solution has been approved, markets in America could react more positively.

# Funds

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Problems in the eurozone, the debt debate in the US and some recent economic figures weaker than expected have once again brought uncertainty to the short term global economic future. Even though we think this uncertainty is just a passing phase and that we will end the year on a positive note, **OUR fixed rate funds in pesos offer total security with stable yields** for getting through these next few months of volatility.

The fiscal problems in countries such as Greece, Ireland, Portugal and most recently Italy, together with the political debate in the United States about raising the debt ceiling for the country have sparked a certain level of nervousness in the markets over the last few weeks. Some analysts are contemplating once again the possibility of falling back into a recession and the feeling in general has changed drastically after disappointing job creation figures in the US. In the face of all this, we are very likely to have a complicated summer with strong movements upwards as well as downwards in the stock markets, interest rates and exchange rates. However, there are two good pieces of news for being optimistic in the short and medium term.

Short term:

Contrary to the past, Mexico has become one of the main targets for investment for large global investors. Our solid public finances, the level of our international reserves, low deficit and controlled inflation have created great stability in our fixed rate instruments such as cetes (Treasury bonds), bonds, promissory notes and fixed rate funds. We think this stability will continue for a long time to come which means that investment in these types of

Funds	Yield 2011*	Yield 2010	Last 12 months*
ACTIMED	3.42%	4.43%	3.62%
LOYPLUS	3.20%	4.86%	3.80%
ALTERNA	3.64%	5.64%	3.95%
APOLO12	4.00%	4.69%	4.07%

\*B3 Series. Net yields on July 15, 2011.  
Past performances do not guarantee future returns.

**Alfa will invest 86.5 million USD in gas wells in the US.** Alfa, the Mexican company that operates plants in 16 countries will invest 86 million 500 thousand dollars this year in the exploration and drilling of gas and oil wells in the United States. This year's plan contemplates the drilling of 120 wells and it hopes to increase this to 140 in 2012. Through its subsidiary Newpek, Alfa has entered into a joint venture with Pioneer Natural Resources in the United States and Reliance Industries in India for the drilling and exploitation of wells in the Edwards and Eagle Ford Shale formations located in a strip of almost 110 miles that runs from northeast to southeast Texas, between San Antonio and Corpus Christie. This area of business was initiated in 2006 when the company partnered with Pioneer to look for natural gas in the Edwards formation because it was cheaper to invest in physical coverage for natural gas than financial coverage. The original project was to exploit 200 wells in the Edwards formation, but after discovering great potential in the Eagle Ford Shale formation, there are plans for 2,000 wells between now and 2020 or 2023. In 2008 the company began operations in the Eagle Ford Shale formation, one of the most important to be discovered in the United States. In order to speed up the development of this last mentioned formation, Newpek and its partner Pioneer Natural Resources sold a 45% interest in it to Reliance Industries. By doing this, Newpek was able to raise 210 million dollars that were reinvested in the business. "This formation (Eagle Ford) has been very successful because we have found oil. In fact 55% of what is produced in this formation is light crude and the rest is gas."

**The CFC approves GMexico's acquisition of GAP .** The Federal Competition Commission (CFC) has given its authorization to Grupo Mexico (GMEXICO) to acquire the shares of Grupo Aeroportuario del Pacifico (GAP), according to a note published on the CFC website. GMEXICO announced its intention to acquire more than 30% of the shares representative of the capital stock of GAP in June through a takeover bid for the shares of the company at a price per share of not more than 50 pesos each. GMEXICO and GAP are currently arguing over the fact that GMEXICO wants to put an additional member on GAP's board of directors when, according to the statutes, the company is only allowed one representative.

instrument will not be at risk.

Medium and long term: Even with the current uncertainty, we feel that the foundations for future economic growth are in place in the United States as well as Japan and some European countries. Companies have cleaned their balances and continue to report strong earnings, constantly strengthening their position. At the same time, the American consumer has been going through a period of getting out of debt since the end of 2008. China doesn't seem to be slowing down at all and we mustn't forget that in 2012 there will be elections in the US and

Mexico, events which should aid economic growth in both countries.

Taking the above into consideration, we recommend that the conservative investor invest in the group's fixed rate funds which will remain stable with positive yields over the coming months (the table below shows how they have performed over the last few months amidst very high financial turbulence). For a more aggressive investor, we recommend our funds of funds which could be benefited during the second half of this year (see last month's edition of Actinews).

### Fund news

As a result of the fusion between Actinver-Lloyd and Actinver Financial, the National Banking and Securities Commission (CNBV) has been visiting the group's offices to carry out a review of our possible management of derivatives. If we receive the authorization (which we think is very likely), all the group's funds will have the option of this type of instrument, which will mainly be used to cover possible risks we see in portfolios and make our funds even safer options for investment.

## Fund Yields

Funds	Yield 2011*	Yield 2010	Monthly average*	Funds	Yield 2011*	Yield 2010	Monthly average*
AWLASA	1.39%	1.72%	0.98%	ACTICOBER			
ACTIREN	1.21%	2.07%	0.80%	In Pesos	-8.94%	-4.47%	1.98%
LOYDMAX	3.10%	4.00%	2.38%	In Dollars	0.38%	1.13%	-2.08%
ACTIMED	3.42%	4.43%	2.15%	ACTIPLU			
LOYPLUS	3.20%	4.86%	2.57%	In Pesos	-7.88%	-1.38%	-0.75%
ALTERNA	3.64%	5.64%	1.01%	In Dollars	1.49%	4.40%	-4.81%
ACTIPLA	3.27%	6.31%	2.56%	ACTIEUR			
ACTIGOB	2.47%	2.76%	2.06%	In Pesos	1.78%	-11.38%	-50.28%
F-GUBER	4.15%	4.43%	4.05%	In Dollars	11.67%	-6.19%	-54.26%
APOLO12	4.00%	4.69%	3.46%	In Euros	1.27%	0.35%	-3.96%
ACTIVCR	1.00%	5.92%	-3.19%	PRUEM			
ACTIVPA	1.50%	5.51%	-3.54%	In Pesos	-2.56%	4.60%	12.85%
ACTIVCO	3.01%	4.20%	0.84%	In Dollars	7.09%	10.74%	8.78%

\*Yields on July 15, 2011. B3 series. Past performances do not guarantee future returns. ACTIGOB GE series

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