

## THE MEXICO EQUITY & INCOME FUND, INC.

### Monthly Message From the Fund's Investment Advisor

Dear Stockholders of the Fund,

Despite lingering North American Free Trade Agreement (NAFTA) concerns and uncertainty generated by the July 2018 presidential elections, the Mexbol Index closed 2017 on a positive note underpinned by robust inflows into equities, resilient consumption, and economic growth, as well as a solid macro framework. The Mexico Equity and Income Fund, Inc. MXE's Net Asset U.S. dollar value return was 11.82% for the one-year period ended December 31, 2017, according to Bloomberg and Thomson Reuters. See *Exhibits 9, 1 & 6 in the \*\*Report on the Economy*.

High uncertainty regarding the prevalence of NAFTA, which caused an abrupt depreciation of the Mexican Peso versus the U.S. Dollar and one of the biggest equity market price swings in 9 years, resulted in the Fund registering a **short-term** -362 basis points underperformance relative to the Mexbol Index for the one-year period ended December 31, 2017, which challenged our value and growth investment approach, and the Fund's turnover was higher than the average for the previous 5-year fiscal periods. See *Exhibit 4 on the \*Fact Sheet*.

**In the long-term**, we have granted the Fund's stockholders a 403 basis points excess annual per year U.S. Dollar return for the 5-year period to December 2017, with a lower standard deviation of 1.24 (See *Exhibit 6 on the Fact Sheet*). Relative to the Fund's tracking error and information ratio, the Fund displays a higher excess return with an average divergence. See *\*Exhibits 5 and 6*.

Mexico's sound public policies and 30 years of commitment to institutional consolidation, reflect resilient, persistent growth, supported by services and manufacturing production levels that have responded quite well to a number of shocks since 2014.

The last 30 years have seen a consolidation of the Mexican middle class along with a new young generation that is receiving a better education and will likely turn out to challenge corruption by punishing the ruling party in the July elections. All said, these will undoubtedly be the most competitive and decisive elections in Mexico's modern history. See *\*\*Exhibits 11 and 12*.

### Investment Strategy and Performance

The Fund's contributors, detractors and sectorial changes, among others, for the one-year period ended December 31, 2017, can be found on the new [Fact Sheet](#) attached to this report. See *\*Exhibits 1, 2 and 3*.

### The Mexican Stock Exchange

The Mexbol Index is currently trading at a 34% discount in dollars compared to pesos, and at a discount of 24% on a last 5-year average P/E basis. Compared to Latam

Indexes, the Mexbol Index trades at discounts of 4% and 5% in terms of LTM P/E and EV/EBITDA, respectively, and its ROIC and ROE are relatively higher. See *\*Exhibits 7, 8 and 10*.

### The Economy

In contrast to bleak growth expectations at the beginning of the year, in 2017, the Mexican economy has posted year on year (YoY) quarterly growth rates of 2.9%, 3.1% and 1.5. A lower third quarter growth rate was due to: (i) two big earthquakes, one measuring 8 on the Richter scale and the largest to hit Mexico in 100 years; and (ii) Hurricane "Harvey", historically the strongest in the Gulf of Mexico where most of the country's port and tourism infrastructure is located. The factors that drove economic growth were: (i) Mexico's trade surplus with the U.S., which could reach US\$70 bn by the end of year compared to the previous year's US\$60 bn; and (ii) consumer growth driven by job creation. The average 2018 growth estimate is 2.2% (from sources such as the IMF, Citibanamex, and the OECD). Banxico maintains its 2.5% projection. (*Please see the full macro report on the Fund's web page*). See *\*\*Exhibits 1 and 2*.

### Factors of uncertainty in 2018

At the time of writing, there appears to have been a radical shift in market sentiment with respect to risk associated with the negotiation of NAFTA. As a result, the July presidential elections have become the focal point for markets in terms of risk, as recent polls show a technical tie between the three main coalitions. Finally, while the effect of the U.S. fiscal reform on Mexico's competitiveness has yet to be determined, it is unlikely to undermine interest in the country among foreign investors.

Thus, we conclude our 2017 message by defining our investment advisory service's main goal as strengthening our in-depth fundamental analysis and human capital in order to continue enhancing our decision-making process.

Yours sincerely,

Eugenia Pichardo  
Portfolio Manager

January 18, 2018

*\*Go to the Fact Sheet*

*\*\*Go to the Report on the Economy*



THE MEXICO EQUITY & INCOME FUND, INC.

RETURNS

As of December 31, 2017	Total Annual Average U.S. Dollar Return through Dec. 31, 2017 (Reinvested Dividends)					
	1 Month	1 Year	3 Years	5 Years	10 Years	Since MXE Inception in 08/30/90
MXE NAV*	-2.49% <sup>1</sup>	11.82% <sup>1</sup>	-3.95% <sup>1</sup>	-0.17% <sup>1</sup>	1.65% <sup>1</sup>	11.71% <sup>2</sup>
MXE NAV (Returns in Mexican Pesos "MXN")	2.89% <sup>3</sup>	6.08% <sup>3</sup>	7.79% <sup>3</sup>	8.55% <sup>3</sup>	7.81% <sup>3</sup>	19.84% <sup>3</sup>
MXE Market Price	-2.49% <sup>1</sup>	12.40% <sup>1</sup>	-4.91% <sup>1</sup>	-0.43% <sup>1</sup>	2.78% <sup>1</sup>	12.01% <sup>2</sup>
MXN Appreciation/ Depreciation	-5.22% <sup>3</sup>	5.41% <sup>3</sup>	-10.89% <sup>3</sup>	-8.04% <sup>3</sup>	-5.71% <sup>3</sup>	-6.78% <sup>3</sup>
MEXBOL Index	-0.67%	15.44%	-3.34%	-4.20%	0.90%	9.67%
MXF NAV	-0.33%	15.73%	-2.41%	-3.25%	0.74%	8.21%
MXF Market Price	0.00%	8.33%	-3.62%	-4.47%	1.68%	8.84%
MXE NAV Excess Return vs. MEXBOL Index	-182	-362	-61	<b>403</b>	75	204

Cumulative to December 31, 2017	(Dividends Reinvested)					
	1 Year	3 Years	5 Years	10 Years	Since MXE Inception 8/30/90	Discount to NAV, as of Dec. 31, 2017
MXE Common Share Market Price	12.40% <sup>1</sup>	-14.01% <sup>1</sup>	-2.15% <sup>1</sup>	31.53% <sup>1</sup>	2118.96% <sup>3</sup>	-13.34%
MXF Common Share Market Price	8.33%	-10.46%	-20.44%	18.09%	912.52%	-12.89%

Source: U.S. Bancorp<sup>1</sup>; Thomson<sup>2</sup>; PAM<sup>3</sup>, Bloomberg.

The Fund's portfolio securities are denominated in Mexican pesos. As a result, the portfolio return in U.S. dollars must increase in market value at a rate in excess of the rate of the decline in the value of the Mexican peso against the U.S. dollar in order to present an excess dollar return.

The NAV accretion that resulted from share repurchases, for the 1, 3, and 5-year period ended November 30, 2017, was 0.00, 0.04, and 0.04 respectively. For the purpose of performance calculation, U.S. Bancorp assumes that MXE's dividends and distributions are reinvested at the closing market price on the dividend ex-date and takes into account the dilution effect resulting from fund's stock dividend. This calculation of MXE's performance figures may differ from other financial sources, such as Bloomberg.

MXE's ratio of expenses to average net assets=1.89% for the annual period ended July 31, 2017.

MXF's ratio of expenses to average net assets=1.69% for the semi-annual ended April 30, 2017.

Performance data quoted represents past performance; past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance of the fund may be lower or higher than the performance quoted.



## THE MEXICO EQUITY & INCOME FUND, INC.

### **DISCLOSURES**

*Pichardo Asset Management, a registered Mexican and U.S. Independent Investment Advisor has prepared this reported based on sources it believed to be accurate and reliable. However, the figures are unaudited and neither the Fund, Pichardo Asset Management (the Investment Advisor), nor any other persons or authorities guarantee their accuracy. Investors should seek their own professional advice and should consider the investment objectives, risks, changes, and expenses before acting on this information. Pichardo Asset Management is a registered investment advisor since 2003 in accordance with Section 204 of the Investment Advisers Act of 1940 and is also registered as an Independent Investment advisor in Mexico pursuant to articles 225 and 226 of the Mexican Securities Act under registration number 30018-001 (5365).*

*Total return figures with distributions reinvested at the dividend reinvestment price are stated net-of-fees and represents past performance. Past performance is not indicative of future results, current performance may be higher or lower. Holdings are subject to change and are provided for informational purposes only and should not be deemed as a recommendation to buy or sell the securities shown.*

#### **Considerations and risks involved in investing in Mexican securities.**

*All investments involve risk. Principal loss is possible. Investing internationally involves additional risks such as currency fluctuations, market prices volatility, social and economic instability, changes in taxation, periods of illiquidity and other factors. Stocks of small-and-mid-capitalization companies involve greater volatility and less liquidity than larger-capitalization companies. All Mexican companies are subject to Mandatory IFRS (International Financial Reporting Standards) accounting since the year 2011.*

*The Fund's portfolio securities are denominated in Mexican pesos. As a result, the portfolio return in U.S. Dollars securities must increase in market value at a rate in excess of the rate of the decline in the value of the Mexican peso against the U.S. dollar in order to present an excess dollar return.*

*To read about the Mexico Equity and Income Fund, Inc. please access the Annual Report by calling (414) 765-4255 to receive a copy, or access the Annual Report on the Funds website [www.mxefund.com](http://www.mxefund.com), under the section caption investor reports. Investors should consider the Fund's investment objectives, risks, charges and expenses carefully before investing. An investment in the Fund should not constitute a complete investment program.*

*Closed-end funds are traded on the secondary market through one of the stock exchanges. The Fund's investment return and principal value will fluctuate so that an investor's shares may be worth more or less than the original cost. Shares of closed-end funds may trade above (a premium) or below (a discount) the net asset value (NAV) of the fund's portfolio and there is no assurance that the fund will achieve its investment objective.*

*For further information please contact Pichardo Asset Management +52 (55) 5261 4613 [imartin@paminversion.com](mailto:imartin@paminversion.com).*

## THE MEXICO EQUITY & INCOME FUND, INC.

### ECONOMIC DATA

- **Gross Domestic Product (GDP):** According to INEGI, the demand side of GDP grew 3.0% in **3Q17**. By components, primary activities increased by 1.0%, secondary activities 0.6%, and tertiary activities 4.1.%
- **Economic Activity Index.** According to INEGI, economic activity (IGAE, a Gross Domestic Product proxy) decreased by 0.1% month over month (m/m) in **October**. In seasonally-adjusted terms, services sector activities increased by 0.4%, industrial sector activities decreased -0.1%, and agricultural sector activities increased 0.1% compared to the previous month.
- **Industrial Activity.** In **November**, industrial production decreased by -0.1% m/m. Seasonally-adjusted data showed that mining was up 0.1%, manufacturing activities increased 0.6%, while utilities grew 5.7%, and construction decreased -1.2% m/m.
- **Gross Fixed Investment.** In **October**, gross fixed investment (GFI) decreased -1.0%, m/m. Expenses related to machinery and equipment decreased -2.6%, and those related to construction decreased by -1.6%, m/m. GFI posted a -3.2% dropped y/y.
- **Trade Balance.** The trade deficit for the first **11 months** of the year was US\$10.718 billion, 18.3% below the US\$13.1 billion recorded in the same 2016 period .
- **Mexican Oil Mix.** As of **end-December**, the price of the Mexican oil mix was USD\$56.19 per barrel, translating into a 4.8517% increase in one month, and a 21.3607% increase in one year.
- **Retail Sales.** Retail decreased -0.1% y/y in **October**. Retail sales increased 1% in relation to the previous month.
- **Unemployment.** The **December** unemployment rate came in at a seasonally-adjusted 3.4%.
- **Monetary Policy.** On **December 14, 2017**, Banco de Mexico maintained its benchmark interest unchanged at 7.25%.
- **Inflation.** The **December** Consumer Price Index (CPI) increased by +0.59% month-over-month. Annual headline inflation came in at 6.77% and core inflation 4.87%.
- **Public Finances:**
  - o Net budgetary expenditure was 6.4 percent lower in real terms vs. the end of the third quarter of 2016 and \$85.1 bn pesos above the budget program. Excluding contributions made in both years using the Bank of Mexico's Excess Operating Liquidity (ROBM) to acquire financial assets and the Federal Government's 2016 contribution to Pemex, net expenditure paid was a real 2.8 percent below the same 2016 period and 11.3 billion pesos below the program.
  - o Public Sector Financial Requirements (RFSP) registered a \$73.341 billion surplus vs. a \$207.657 billion deficit for the same period in 2016.

Source: SHCP, BANXICO, INEGI.

**THE MEXICO EQUITY & INCOME FUND, INC.**

**ECONOMIC PROJECTIONS**

<b>Economic Projections</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017e</b>	<b>2018e</b>
<b>National Accounts</b>					
Real GDP growth (y/y)	2.3%	2.5%	2.9%	2.5%	2.7%
GDP (US \$bn.)	1.288	1.139	1.076	1.181	1.321
Consumption (Chg. y/y)	2.0%	3.3%	2.4%	2.4%	2.5%
Investment (Chg. y/y)	2.3%	4.5%	1.1%	1.0%	3.7%
Exports (Chg. y/y)	7.3%	9.4%	3.5%	7.6%	8.9%
Imports (Chg. y/y)	5.7%	6.1%	2.9%	5.3%	7.9%
<b>Monetary and Exchange Rate Ind.</b>					
CPI Inflation (year-end)	4.1%	2.1%	3.3%	6.3%	3.8%
US\$ Exchange Rate (year-end)	14.7	17.2	20.6	18.9	19.0
28Day Cetes Int. Rate (year-end)	3.00%	3.25%	5.75%	7.0%	6.5%
<b>Balance of Payments</b>					
Trade Balance (US\$ bn.)	-2.8	-14.5	-13.1	-14.4	-12.4
Exports (US\$ bn.)	397.5	380.8	373.9	397.8	424.5
Imports (US\$ bn.)	400.0	395.2	387.06	412.2	436.9
Transfers (US\$ bn.)	23.6	24.8	26.6	n/a	n/a
Current Account (US\$ bn.)	-24.8	-32.4	-27.8	-23.4	-27.8
Foreign Direct Inv. (US\$ bn.)	25.6	28.4	26.7	n/a	n/a
<b>Debt Profile</b>					
International Reserves (US\$ bn.)	193.2	176.7	176.5	178.0	180.0
Public Debt (gross % of GDP)	41.0%	42.5%	50.5%	48.0%	48.0%
External Debt (gross % of GDP)	11.9%	19.7%	15.5%	15.2%	15.0%

Source: SHCP, BANXICO, INEGI, Santander.

The projections on this page are based on industry estimates and are no guarantee of future outcomes.



## THE MEXICO EQUITY & INCOME FUND, INC.

### DEFINITIONS

- **Banco de Mexico (Banxico):** The Central Bank of Mexico.
- **Basis Points:** Refers to a common unit of measure for interest rates and other percentages in finance.
- **The Consumer Price Index (CPI):** Is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care.
- **EV/EBITDA:** Is a ratio used to determine the value of a company.
- **EWV:** The iShares MSCI Mexico ETF seeks to track the investment results of a broad-based composed of Mexican equities.
- **Foreign Direct Investment (FDI):** Foreign direct investment (FDI) is an investment made by a company or individual in one country in business interests in another country, in the form of either establishing business operations or acquiring business assets in the other country, such as ownership or controlling interest in a foreign company.
- **LATAM Indexes:** Captures market capitalization across countries in Latin America.
- **Information ratio (IR):** Measures a portfolio manager's ability to generate excess returns relative to a benchmark.
- **Mexbol Index:** The Mexican Bolsa Index, or the IPyC (Indice de Precios y Cotizaciones), is a capitalization-weighted index of the leading stocks traded on the Mexican Stock Exchange. The index was developed with a base level of 0.78 on October 30, 1978.
- **P/E:** The price-earnings ratio (P/E ratio) is the ratio for valuing a company that measures its current share price relative to its per-share earnings.
- **PAN:** National Action Party
- **PRI:** Institutional Revolutionary Party
- **PRD:** Party of the Democratic Revolution
- **PT:** The Labor Party
- **PES:** The Social Encounter Party
- **Return on Equity (ROE):** Is the amount of net income returned as a percentage of shareholders equity.
- **Return on Invested Capital (ROIC):** A calculation used to assess a company's efficiency at allocating the capital under its control to profitable investments.
- **Standard & Poors (S&P):** Standard & Poor's (S&P) is the world's leading index provider and the foremost source of independent credit ratings. Standard & Poor's has been providing financial market intelligence to decision makers for more than 150 years.
- **The International Monetary Fund (IMF):** The International Monetary Fund is an international organization that aims to promote global economic growth and financial stability, to encourage international trade, and to reduce poverty.
- **The North American Free Trade Agreement (NAFTA):** A regulation implemented January 1, 1994 in Mexico, Canada and the United States to eliminate most tariffs on trade between these nations. The three countries phased out numerous tariffs, (with a focus on those related to agriculture, textiles and automobiles), between the agreement's implementation and January 1, 2008. NAFTA's purpose is to encourage economic activity between the United States, Mexico and Canada.
- **The Organization for Economic Development and Cooperation (OECD):** An intergovernmental economic organization with 35 member countries, founded in 1960 to stimulate economic progress and world trade. It is a forum of countries describing themselves as committed to democracy and the market economy, providing a platform to compare policy experiences, seeking answers to common problems, identify good practices and coordinate domestic and international policies of its members.
- **The World Trade Organization (WTO):** An intergovernmental organization that regulates international trade. The WTO officially commenced on 1 January 1995 under the Marrakesh Agreement, signed by 123 nations on 15 April 1994, replacing the General Agreement on Tariffs and Trade (GATT), which commenced in 1948. It is the largest international economic organization in the world. The WTO deals with regulation of trade in goods, services and intellectual property between participating countries by providing a framework for negotiating trade agreements and a dispute resolution process aimed at enforcing participants' adherence to WTO agreements, which are signed by representatives of member governments, and ratified by their parliaments.