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Mexico: Summary Of Developments Surrounding Negotiations Toward Reducing Foreign Debt Burden

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On the evening of April 12, Finance Secretary Pedro Aspe announced that his government had reached an agreement with the International Monetary Fund for a $3.6 billion loan to be disbursed over a three-year period. Unidentified Mexican officials cited in the national and foreign media said that about 30% of the loan will be set aside for reduction of the country's foreign debt. According to some officials, by publicly expressing a desire for a "substantial" amount of debt reduction, IMF officials are deliberately putting pressure on the banks to adopt rapid and effective measures to provide debt relief. As reported by the Washington Post (04/13/89), the IMF's $3.6 billion is part of a larger loan-plus-debt reduction package, the size of which is unclear. The additional components of the package may include $500 million in IMF financing to compensate for losses resulting from low oil prices; $1.5 billion in World Bank loans for specific sectoral projects; a portion of the $4.5 billion of Tokyo's overall commitment to the debt reduction strategy proposed by US Treasury Secretary Nicholas Brady; loans Mexico may be able to obtain from the Paris Club; and, funds Mexico City may receive from other sources. Unidentified officials told the Post that once the Fund's executive board approves the $3.6 billion package for Mexico, the Fund will proceed with disbursing money before Mexico negotiates new arrangements with commercial bank creditors. The sources said the 30% set-aside could be used by Mexico either to buy back some of its debt at a reduced price, or as collateral for a new bond that banks would receive in exchange for old loans. During a hearing before a House appropriations subcommittee on April 17, Secretary Brady said negotiations between Mexico and its bank creditors will most certainly be quite "prolonged." According to Notimex, in contrast to the reported expectations of Mexican officials, Brady said that the IMF will not disburse any funds to Mexico until the government has reached an agreement with its private bank creditors. In an interview with Notimex on April 18 in Washington, Harvard economics professor Jeffrey Sachs said Mexico must not bow to foreign pressure in negotiations to reduce its foreign debt burden with the creditor bank committee. Sachs was interviewed shortly after he testified at a congressional subcommittee hearing on the foreign debt issue. The professor has served as a consultant to the Bolivian government on foreign debt payment strategies and related economic policy matters. At present, Sachs acts as an adviser to the United Nations on macroeconomic affairs. According to Sachs, a 20% reduction in Mexico's foreign debt obligations is insufficient to achieve economic recovery. He said, "The worst mistake we can make is to apply strong pressure on Mexico to accept a 20% reduction in its debt in negotiations with commercial banks...The best we can do is give them the necessary time to negotiate." Regarding the timing of an eventual broad-based agreement between the banks and Mexico City, Sachs said, "I do not believe there will be results [in the negotiations between Mexico and the committee of creditor banks] before July." Mexican officials and the New York-based committee representing Mexico's foreign commercial bank creditors commenced negotiations on April 19. Mexican officials, according to the New York Times (04/19/89) continue to be convinced that the recent IMF agreement will provide leverage to reduce its annual debt service burden by as much as two-thirds. Unidentified officials said the Fund was willing to disburse the initial installment of a $3.6 billion package independent

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of an agreement with the commercial banks. Mexico City hopes to reduce the total outflow of debt payments to less than 2% of GDP from 6%, or to less than $3.5 billion from $10 billion per year. The Mexican government estimates its total foreign debt obligations at $100.4 billion, of which $60 billion is owed to commercial banks. Among the options presented by Mexico are the exchange of $30 billion of bank debt into bonds with a lower face value (determined in part by prices of debt paper in the secondary market), but with market interest rates. Another $10 billion of bank debt might be exchanged for bonds with an equal face value, and bearing much lower interest rates than the bank loans. Unidentified bankers told the Times that the viability of these options depends on the extent to which Mexico can use money from the IMF and World Bank to provide guarantees on the bank loans. Other options are debt-equity swaps and postponement of amortization payments. The Mexican government has estimated annual financing needs will run about $7 billion a year for the next few years. (Basic data from Washington Post, 04/13/89; AP, 04/17/89; Notimex, 04/18/89; Xinhua, New York Times, 04/19/89)

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