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LADB Staff

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by LADB Staff
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A surge of foreign investment has significantly raised the amount of foreign reserves in Mexico, leading the government to optimistically predict that supplies are sufficient to cover all obligations in Treasury Bonds (Tesobonos) for the rest of the year. According to government statistics, Mexico's reserves of foreign currency stood at US$14.35 billion as of mid-July. In fact, reserves increased by about US$4.3 billion in the course of one week in mid-July because of the disbursement of loan guarantees of US$2.5 billion from the US and about US$2 billion from the International Monetary Fund (IMF). The US and IMF loan guarantees are part of the US$50 billion rescue package for the Mexican economy, put together by US President Bill Clinton's administration in January (see SourceMex, 02/01/95).

The current level of foreign reserves in Mexico is close to the US$17 billion announced in October of last year. Indeed, reserves have recovered significantly from the US$2 billion Mexico had after the crisis broke out in December. Additionally, reserves are now more than sufficient to meet pending Tesobono obligations of US$9.788 billion due to mature before the end of the year. Of this total, roughly US$6.6 billion will mature by the end of August.

According to Finance Secretary Guillermo Ortiz Martinez, the Mexican government has retired about US$30 billion in pending Tesobono obligations since the start of the year. In interviews with El Norte and Reforma daily newspapers, economic analysts said the main advantage of Mexico's newly found solvency is the psychological boost to the economy and increased stability for the peso. Indeed, the Mexican Stock Exchange (BMV) has shown signs of rallying. In mid-July, the BMV's main index (Indice de Precios de Cotizacion, IPC) reached 2,531.49, almost 1,000 points above the post-devaluation low of 1,447.52 set in February of this year. On July 18, the IPC had bounced back to 2,479.62 points.

Still, market analysts cautioned that despite the BMV's recovery in terms of points, the market has lost about 18% from its dollar value since December. Additionally, they said the latest recovery at the BMV was as much a function of lower US interest rates as renewed confidence in Mexico's macroeconomic picture. The peso, meantime, stood at 6.06 nuevo pesos per US$1.00 on July 18, compared with 7.45 nuevo pesos per US$1.00 in March. In a meeting with a group of directors for the Associated Press in mid-July, Zedillo projected that the peso would remain stable at close to 6.00 nuevo pesos per US$1.00 the rest of the year. Still, even though Mexico's economy has shown some signs of recovery an increase in the trade surplus, a gradual decline in inflation, and a reduction in interest rates many other factors could derail a long-term recovery. These include a surge in the jobless rate, a shaky banking system, and a sharp contraction of the economy.

According to government forecasts, Mexico's GDP is expected to decline by 2% this year, although many private economists have projected a fall in GDP of as much as 5.2%. Another strong concern,

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according to many economists, is that the Zedillo administration has been forced to rely on an increase in the value-added tax (impuesto al valor agregado, IVA) and on the issuance of short-term financial instruments such as Treasury bonds to raise revenues. Indeed, in mid-July members of Zedillo's own Institutional Revolutionary Party (PRI) expressed strong reservations about the government's strategy of financing the economic recovery through the issue of new financial instruments with high interest rates. For example, during a hearing in mid-July, Deputy Francisco Suarez Davila, chairman of the finance committee in the Chamber of Deputies, pointed out that the only reason Mexico has been able to survive the recent economic crisis was international support from the US, the World Bank, and other multilateral institutions. Suarez warned that Mexico could find itself in the same situation in coming years should reserves of foreign currency tighten again.

On July 12, the Mexican government successfully auctioned off US$1 billion in two-year Treasury notes. This was the first successful placement of financial instruments on international markets since the devaluation of the peso in December. However, analysts noted that the issue offered a relatively high interest rate of 5.375% over the six-month London Interbank Offered Rate, a sign that Mexican debt continues to be seen as a risky investment. Still, the Zedillo administration appears to have few options available to fund the country's economic recovery in the short term other than to issue financial instruments on international markets at high interest rates. A study produced by the private think tank Centro de Estudios Economicos del Sector Private (CEESP) showed that the savings rate in Mexico has fallen steadily since 1982, thus contributing to the country's precarious economic position. The CEESP study, conducted for the Mexican Bankers Association (ABM), recommended that the Zedillo administration continue to look for ways to encourage an increase in the savings rate.

"The government has to develop programs to encourage long-term savings, since this is the only way to accumulate needed resources in sufficient volumes to support sustained growth," read the study. According to some analysts, the government itself is to blame for the lack of savings, since current savings schemes do not offer safeguards for investments against such risks as the peso devaluation. The one savings scheme that has had mild success is the retirement savings system (Sistema de Ahorro para el Retiro, SAR). Even so, the funds gained through the SAR constitute only 2.3% of Mexico's GDP.

In comparison, Chile, whose economic recovery was financed in strong part by domestic savings, boasts that its retirement funds represent 34% of the country's GDP, according to the CEESP study. Ironically, according to statistics compiled by the US Federal Reserve Bank, Mexican nationals deposited US$4.2 billion in US banks in January and February of this year, the first two full months following the devaluation of the peso. In fact, analysts said the total placed by Mexicans in US banks in January-February was 20% higher than the US$3.5 billion in foreign reserves available to the Mexican government during January.

Additionally, the transfer of funds during the first two months of the year to US banks brought total deposits by Mexican nationals in the US to US$12.6 billion as of the end of February. According to the US Federal Reserve report, the US$16.7 billion in US accounts as of the end of February represented more than one-fifth of the US$76 billion placed by Latin Americans in US banks as of that period. The report also noted that almost 70% of the total of US$76 billion came from four

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countries: Mexico, Venezuela, Brazil, and Argentina. (Sources: Agence France-Presse, Deutsche Press Agentur, El Economista, 07/11/95; Wall Street Journal, 07/12/95; El Financiero, 07/14/95; Notimex, 07/11/95, 07/17/95; La Jornada, 07/11/95, 07/17/95, 07/18/95; New York Times, El Norte, 07/17/95; Reuter, 07/17/95; Associated Press, 07/12/95, 07/18/95)

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