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## **Banking Consortium Awards Mexico US\$2.5 Billion Contingency Line of Credit**

by LADB Staff

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In early November, an international consortium of 31 banks and brokerage houses announced the creation of a special credit line of US\$2.5 billion for Mexico to use in case of emergencies caused by turbulence in global financial markets. The consortium includes financial institutions from the US, Japan, and several European and Latin American countries. Among them are some of the largest and most prominent banks in the world, including Banco Bilbao Vizcaya, Citibank, Chase Manhattan Bank, Banque Paribas, Credit Lyonnais, ABN AMRO Bank, Fuji Bank, Bank of Japan, Deutsche Bank, and the Royal Bank of Canada. Participating brokerages include Lehman Brothers, Merrill Lynch, Morgan Stanley, and Daiwa Securities.

### ***Government says credit will only be used in emergencies***

According to the Secretaria de Hacienda y Credito Publico (SHCP), the new line of credit is only a precaution to ensure that Mexico is prepared to deal with another international crisis. One SHCP spokesperson said the consortium offered the most favorable interest rates currently available in global markets. The line of credit line was created for a period of one year, to November 1998, and is renewable for another year at that time. "With this operation, the federal government reduced the risk in financing its debt, obtained protection against international volatility, reduced the risk of external shocks on Mexico, and maintained orderly access to international capital markets," said the SHCP spokesperson.

The SHCP will also be allowed to use the credit to cover any gaps resulting from an unexpected decline in federal government revenues or increases in public-spending costs caused by "external factors," such as higher international interest rates or a drop in prices for oil exports. Crisis in global financial markets has ripple effect on Mexico. The new credit line was announced less than two weeks after a plunge in the Hong Kong stock market caused sharp declines in other financial markets around the world, including Mexico's Bolsa Mexicana de Valores (BMV). The BMV's main index (Indice de Precios y Cotizaciones, IPC) fell by almost 10% in the days following the crisis in Hong Kong.

The impact of the financial crisis was more evident in the foreign currency markets, where the Mexican peso declined to 8.65 pesos per US\$1.00 before recovering to 8.32 pesos per US\$1.00 by mid-November. Before the Hong Kong crisis, the Mexican currency was trading at about 7.75 pesos per US\$1.00. To bolster the peso, the Banco de Mexico (central bank) was forced to intervene in the foreign-currency markets, selling almost US\$6 billion since Oct. 27.

According to the SHCP, the line of credit provided by the 31 banks is intended to prevent a recurrence of the fiscal crisis that followed the devaluation of the peso in December 1994. The 1994 peso devaluation caused capital flight and a sharp reduction in Mexico's foreign-currency reserves. To deal with that situation, the government was forced to borrow US\$50 billion from the

US and several multilateral institutions, including the International Monetary Fund (see SourceMex, 03/15/95). The access to US and international funds helped the government stabilize economy, although the crisis prevented Mexico from obtaining additional funds from global capital markets. Speaking to reporters, deputy finance secretary Martin Werner pointed out that conditions are very different now than during the 1994 devaluation, since Mexico currently has much larger currency reserves and a much smaller debt. Werner said Mexico's currency reserves as of October stood at US\$25.5 billion, compared with only US\$3.5 billion in 1994.

Similarly, Mexico's foreign debt is now only US\$5 billion, compared with US\$40 billion three years ago. For his part, SHCP spokesperson Alejandro Valenzuela pointed out that a higher percentage of the capital placed by foreigners in Mexico has taken the form of direct investment rather than indirect investments in money markets. According to Valenzuela, direct foreign investment accounts for US\$12 billion of the US\$16 billion of foreign capital placed in Mexico so far this year.

Still, the crisis in the Hong Kong market forced the Mexican government to take extra precautions. For example, in early November the SHCP suspended all new bond issues on international markets. Government officials have also expressed concern about other repercussions, such as a reduction in foreign currency reserves. According to the Banco de Mexico, reserves declined by a net US \$144 million between Oct. 31 and Nov. 7 as a direct result of the global financial crisis. (Sources: El Financiero International, 11/03/97; Novedades, 11/07/97; La Jornada, 10/31/97, 11/07/97; Reuter, 11/09/97; The News, 10/17/97, 11/10/97; Excelsior, 10/29/97, 11/10/97; El Universal, 11/03/97, 11/07/97, 11/10/97)

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