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Mexico's currency has lost more than 25% of its value so far this year, prompting the Banco de Mexico (central bank) to reduce the supply of pesos available to the economy. In mid- August, the central bank announced plans to reduce liquidity by 70 million pesos (US$7 million) per day, which would slow the flight of capital from Mexico. As of Sept. 2, the Mexican currency was quoted at 9.96 pesos per US$1.00, after declining to as much as 10.20 pesos per US$1.00 on Sept. 1. In contrast, the Mexican currency was trading at 7.76 pesos per US$1.00 in early September 1997 and at 8.06 pesos per US$1.00 at the start of this year.

Economists said the central bank's move to reduce liquidity will also contribute to higher interest rates and a reduction in GDP growth this year. Immediately after the central bank decision in mid-August, interest rates for 28-day Treasury Certificates (Certificados de Tesoreria, CETES) surged to 22%, compared with 18.9% in early August.

The central bank's action was followed by widespread rumors that Banco de Mexico chief governor Guillermo Ortiz Martinez was about to tender his resignation. The rumors contributed to a sharp decline in the main index (Indice de Precios y Cotizaciones, IPC) at the Bolsa Mexicana de Valores (BMV) on Aug. 25. The central bank denied the rumors, but this failed to reassure the Mexican markets, which remain at the mercy of unstable Asian and Russian financial markets.

Economic growth to slow in second half of 1998

Some economists have forecast a slowdown in the Mexican economy during the second half of this year because of the increase in interest rates and the continuing weakness in global oil prices. Jaime Collazo of the Instituto Mexicano de Ejecutivos de Finanzas projects the GDP growth rate for July-December at 3% or less, compared with the 5.3% rate reported for the first half of the year. Clemente Ruiz Duran, an economist at Universidad Nacional Autonoma de Mexico (UNAM), said the reduced growth rate for the second half of the year will be reflected in a scarcity of new jobs.

Meanwhile, the high inflation rate is threatening the government's targets for annual inflation this year. Other economists said Mexico's economic growth could be hampered further if the government is forced to make a fourth reduction in the federal budget this year. The administration already cut federal expenditures three times this year because of weak global oil prices, which have reduced Mexico's oil- export revenues significantly (see SourceMex, 01/21/98, 03/25/98, 07/15/98).

In his State of the Union address Sept. 1, President Ernesto Zedillo acknowledged that the Mexican economy faces extreme difficulties in the coming months because of the continued weakness in the global oil market and the ongoing instability of the Asian and Russian economies. "I must be the first to warn that the circumstances in which our economy will operate in the near future will be

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difficult," Zedillo said in his address. Zedillo also defended the government's proposal to create the bank-rescue fund (Fondo Bancario de Proteccion al Ahorro, FOBAPROA) following the devaluation of the peso in December 1994.

In March of this year, Zedillo's banking-reform legislative package included a proposal for the government to incorporate the FOBAPROA liabilities into the public debt. This proposal has been strongly opposed by the center-left Partido de la Revolucion Democratica (PRD) and the conservative Partido Accion Nacional (PAN), which accuse the administration of passing on the debts of wealthy bankers and other business owners to taxpayers. The two parties have offered their own proposals, which include forcing bankers and business owners who benefitted from the program to assume a large percentage of the FOBAPROA liabilities (see SourceMex, 04/15/98, 07/22/98 and 08/26/98)

The PRD organized a nonbinding referendum scheduled only two days before the president's annual speech. According to party leaders, 96% of the 3 million Mexicans who participated rejected the administration's proposal to incorporate FOBAPROA liabilities into the public debt. "Based on this mandate, the party and its legislators will act with responsibility with respect to the people and the nation," said PRD president Andres Manuel Lopez Obrador. [Note: Peso-dollar conversions in this article are based on the Interbank rate in effect on Sept. 2, reported at 9.96 pesos per US$1.00] (Sources: Los Angeles Times, 08/30/98; El Economista, 08/26/98, 08/31/98; La Jornada, 08/31/98; Novedades, 08/24/98, 08/27/98, 08/31/98, 09/01/98; Spanish news service EFE, The Dallas Morning News, The Miami Herald, 09/01/98; Excelsior, 08/26/98, 08/31/98, 09/02/98; El Universal, 08/18/98, 08/28/98, 08/31/98, 09/01/98, 09/02/98; Reuters, 08/31/98, 09/02/98; Associated Press, 09/02/98; The New York Times, 09/02/98)

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