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President Ernesto Zedillo's administration will reduce its budget projections for 1999 because of the continuing slump in global oil markets. Mexican crude-oil prices, which have been deteriorating steadily since the end of 1997, reached their lowest level in 25 years in recent weeks. On Dec. 4, Mexican crude-oil prices were quoted as low as US$7.50 per barrel, compared with US$13.50 per barrel at the beginning of 1998. The severe decline in oil prices was caused in part by the inability of the Organization of Petroleum Exporting Countries (OPEC) to agree to limit production at a meeting in Austria in late November. Mexico, along with Saudi Arabia and Venezuela, led an initiative last year to convince oil producers to reduce supplies of crude oil on global markets (see SourceMex, 03/25/98, 06/10/98).

The prospect that oil prices will remain weak led the Zedillo administration to revise its original budget proposal for 1999, which had been submitted to the Chamber of Deputies for approval in early November. In the original budget, the administration had set public expenditures at 1 trillion pesos (US$105 billion), based on projected oil prices of between US$11.00 and US$11.50 per barrel.

The original budget proposal, considered the most austere in 20 years, eliminated subsidies for tortillas and imposed surcharges on gasoline and telephone services. The budget set public expenditures at 15% of GDP in 1999, compared with about 15.7% in 1998 (see SourceMex, 11/11/98). With oil-export revenues expected to decline, public expenditures next year will be reduced to less than 15% of GDP. The administration is now projecting average prices for oil exports at between US $9.50 and US$10.00 per barrel, which will reduce revenues obtained from oil exports by between US $850 million and US$1.7 billion.

While the Mexican government has attempted to reduce its reliance on the global oil market, export revenues from crude oil still account for roughly one-third of Mexico's public- sector revenues. The reduction in the budget projection is aimed at averting budget reductions during the year. The administration reduced the 1998 budget three times because of lower-than-expected oil-export revenues (see SourceMex, 01/21/98, 03/25/98, 07/15/98). "I would say that for fiscal prudence, you don't want to change your fiscal budget every time oil moves," analyst Rafael Quijano of Latin American Petroleum Services told Reuters news service. By law, the Chamber of Deputies and Senate, which have been considering the administration's original proposal, must approve the amended budget by Dec. 15.

Because of the tight time frame, the administration and the Chamber of Deputies will be working jointly to cut expenditures. In announcing the reduction, the administration pledged to leave intact expenditures for education and anti-poverty programs. Sen. Rodolfo Becerril Straffon of the governing Partido Revolucionario Institucional (PRI) said some cuts are contemplated for the Secretaria de Turismo (SECTUR), Secretaria de Reforma Agraria (SRA), and other small secretariats.

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PRD seeks to eliminate bank-rescue funds

Becerril said PRI legislators and the Zedillo administration have no immediate plans to reduce the 18 billion pesos (US$1.89 million) allocated next year to bail out the bank-rescue program (Fondo Bancario de Proteccion al Ahorro, FOBAPROA). The decision to leave FOBAPROA funding intact could create a dispute with the opposition parties, which could jeopardize passage of the budget by the Dec. 15 deadline. In its proposal for the budget revisions, the center-left Partido de la Revolucion Democratica (PRD) said the government could more than compensate for falling oil-export revenues by eliminating funding for the FOBAPROA rescue and suspending some payments on Mexico's foreign debt.

Further cuts proposed for state-run oil company The downward revision in the 1999 budget could have major implications for the state-run oil company PEMEX, which has been instructed to suspend US$1 billion in expenditures on major projects next year.

PEMEX director Adrian Lajous said the suspended projects include development of oil-exploration sites on the Tabasco state coast and the implementation of a system of secondary oil recovery. "We will resume these two important projects once PEMEX is able to generate more resources," said Lajous. PEMEX officials said the company has also suspended modernization of the Madero, Tula, and Salmanaca refineries but will proceed with the upgrade of the Cadereyta facility.

Energy Secretary Luis Tellez said PEMEX had hoped to use income from oil exports to finance nearly 42% of its planned investment of 93 billion pesos (US$9.78 million) for next year. The company will now have to make up for some of that revenue by issuing bonds on international markets, said Tellez. In addition to spending cuts, the budget revision could force the government to raise taxes. In an interview with the daily newspaper Excelsior, deputy finance secretaries Tomas Ruiz and Santiago Levy said the executive and legislative branches would have to make some difficult decisions, including possibly raising the value-added tax (impuesto al valor agregado, IVA) from its current rate of 15%.

Many legislators, including the PRI delegation, remain staunchly opposed to increasing the IVA. Legislators of all parties have supported the administration's proposal to implement a 15% tax on telephone service. Members of the PRD said they would support such a tax as long as lower-income users are exempt. As expected, the Camara Nacional de la Industria Electronica, Telefonica e Informatica (CANIETI) and the Sindicato de Telefonistas de la Republica Mexicana (STRM) have come out in opposition of the telephone tax. Macroeconomic projections also revised The administration is also expected to modify its macroeconomic projections for next year.

Under the original budget, the Zedillo government had forecast GDP growth of 3% and an annual inflation rate of 13%. But sources at the Secretaria de Hacienda y Credito Publico (SHCP) say the GDP growth rate will be revised downward to 2.6%, while the target for annual inflation will be increased by one percentage point to 14%. In its original budget, the administration had also targeted a fiscal deficit of only 1.25% of GDP. The latest revisions, however, could push the fiscal deficit to 2% of GDP, SHCP sources told the daily business newspaper El Economista.

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The government's effort to maintain a tight fiscal deficit is expected to keep interest rates at high levels. "Rates will be higher, possibly between 35% and 40%, and will stay high throughout the year," said Sergio Garcia of Value brokerage house in Mexico City. [Note: Peso-dollar conversions in this article are based on the Interbank rate in effect on Dec. 9, reported at 9.95 pesos per US$1.00] (Sources: Bloomberg news service, 12/07/98; Excelsior, 11/25/98, 11/30/98, 12/01/98, 12/02/98, 12/03/98, 12/07-09/98; Novedades, 11/25/98, 11/30/98, 12/03/98, 12/07-09/98; El Financiero International, 12/07/98; El Universal, 11/25/98, 12/02/98, 12/07-09/98; Reuters, 11/26/98, 11/30/98, 12/04/98, 12/07/98, 12/08/98; El Economista, 11/30/98, 12/01/98, 12/03/98, 12/04/98, 12/07-09/98; La Jornada, 12/02/98, 12/05/98, 12/07-09/98; Associated Press, 12/04/98, 12/09/98; The News, 12/07-09/98)

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