## 1. ECONOMIC POLICY

Over the past four years, Mexican economic policy has featured a tough anti-inflation program involving government, labour unions and business in an economic pact that has combined traditional austerity measures (tight fiscal policy) and unorthodox measures (wage, price and exchange rate controls). This policy has been combined with a broad liberalization of the economy, replacing government controls and interference with market forces and foreign competition.

The Economic Pact, in place since 1988 among government, labour and business, has been an important model for the government in its campaign to reduce inflation. The new phase (called Pact for Stabilization, Competitiveness and Employment) has been extended to December 1993 and its principal provision creates a wider band for exchange rate fluctuations. Thus peso devaluations against the U.S.$ will increase from 20 to 40 centavos daily, or 4.8 percent annually. Other provisions in the Pact are monthly increases in the price of energy equivalent to no more than 10 percent annually and a 7 percent increase in the minimum wage (the same as the inflation target for 1993). Labour leaders agreed that other wage settlements in 1993 will not surpass 10 percent.

Although one important economic goal for 1992 was to reduce inflation to less than 10 percent, the final figure was 11.9 percent, compared with 18.8 percent in 1991. The Mexican government is taking extraordinary measures to reduce inflation further, even at the cost of lower economic growth (2.6 percent in 1992 and an estimated 2 percent for 1993). In 1992, the government reduced the value-added tax by five percentage points. The government has also been enforcing price controls and price reduction agreements with the private sector in many goods and services as well as vigilantly collecting income taxes.

In 1992, Mexico experienced a serious deficit of U.S.$22.8 billion in its current account of balance of payments, compared with U.S.$13.8 billion in 1991. In 1992, capital inflows covered this deficit and increased monetary reserves to a record high of U.S.$18.5 billion. In 1992, the pace of foreign capital inflows decreased slightly and the stock market began to fall in the second half of the year. As a result, the government had to increase interest rates to protect against capital flight. The challenge for 1993 will be to continue to keep sufficient flows of foreign capital while maintaining high reserves without choking the domestic economy.

Although the economic goals in 1992 of reduced inflation and sustained economic growth were not fully realized, public finances achieved the targeted surplus and exchange rate parity stability was maintained. The government has also been successful in improving the living standards of the poorest segments of society by means of the government's Solidarity Program.

In November, the 1993 government budget was presented to the Mexican Congress. The budget defined the year's economic policy goals, the most important of which is to achieve single-digit inflation through a continuation of strong austerity measures.

## 2. EXTERNAL DEBT

New authorized public debt for 1993 will be U.S.$3.5 billion.

Although, in May 1992, the Mexican government announced the repurchase of U.S.$7 billion of old debt, total external debt outstanding at the end of 1992 was U.S.$98.9 billion, close to the debt outstanding in October 1982 when Mexico suspended interest payments to banks. External debt has increased mainly because of private sector return to international money markets. However, the debt repurchase will save Mexico U.S.$400 million annually in interest payments.

In February 1990, the Mexican government signed an agreement (the Brady Plan) for debt reduction and for new money from commercial banks. The Institute of International Finances estimates that Mexico paid U.S.$14.2 billion for its external debt service in 1992: U.S.$7.8 billion in principal and U.S.$6.4 billion in interest payments. Although down from 40 percent, this debt reservicing still represents 30.1 percent of Mexico's foreign exchange income from goods and services. The successful negotiation continues to bring confidence to the country and provides psychological reinforcement for capital repatriation and new foreign investment.