Mexico's debt crisis means bold measures are needed now

by Jorge Bazúa

After more than three years of enormous sacrifice to service Mexico's foreign debt—and shore up the collapsing financial structure of the international banks—the raw reality has finally surfaced in the consciousness of every Mexican that all the sacrifice has been in vain, and that Mexico has returned to the same choice that faced it in 1982: to declare a debt moratorium or further bleed its internal economy to keep the international financial institutions solvent.

However, unlike 1982, Mexico today is already so bled dry that it has no margin—political or economic—within which to maneuver, no fat from which to squeeze the "liquidity" in order to service the debt, as in 1983. This time the country is simply incapable of meeting interest payments on its debt.

Through the collapse of oil prices, Mexico will lose one-third of its export income this year, and nearly one-seventh of total public-sector income. Given the levels of austerity under which the country has been operatiang for the past three years, any attempt to absorb the loss of income through import and public expense cutbacks—as the international banks demand—would cause economic contraction beyond the country's limits of endurance.

The first effects of the oil price collapse were felt as of the first three months of this year when the trade balance (exports minus imports) declined precipitously, reaching a mere $782 million, or *60% less than the same period last year*. At the same time, interest payments on the debt for that first trimester of the year absorbed $2.272 billion, an amount met only by reducing the central bank's foreign-exchange reserves. At the same time, economic activity began to contract as a result of the foreign-exchange shortage.

The Mexican government has made strenuous efforts during the past three months to reach a deal with the International Monetary Fund and creditor banks regarding payment of debt service and contracting new credits, all the while demanding a reduction in interest rates and co-responsibility of the banks in dealing with the debt problem. The response of the banks has been brutal. Despite its former "exemplary and responsible" behavior in dismantling its economy, Mexico has fallen from the bankers' grace.

New austerity measures and economic shrinkage, the privatization of state enterprises, the exchange of national assets for debt, opening up to foreign investment and other such measures are the conditions demanded of Mexico before the bankers would consider granting a penny in new loans so urgently needed by Mexico to both compensate for the fall in oil prices and maintain its debt-service payments.

Under these conditions, Mexican President Miguel de la Madrid has been left with little choice. On June 2, de la Madrid declared, "We are going to overcome the crisis through growth, and not stagnation. We are going to continue fighting inflation, but without frustrating development. We are going to meet financial obligations in accordance with the country's real ability to pay and without strangling the nation's productive apparatus. This capacity to pay—our creditors must be made to understand—can only be maintained and even enhanced (and in this their interests coincide with ours) to the extent that Mexico is allowed to continue growing. There are no dead debtors nor bankrupt clients."

Only 10% for the debt

Everything indicates that Mexico will adopt the Peruvian strategy, in the sense of limiting debt service payments to a fixed percentage of its export income. In high-level government circles, the possibility of setting a 25% ceiling has been discussed, which, if applied to the totality of income from export of goods and services, would mean allocating a little more than $5 billion to servicing the debt—nearly half of what the banks are demanding in interest and principal payments. But the reality is that Mexico could not meet even that percentage of payments without further destruction of its national economy.

The statistics speak for themselves. Mexico hopes to receive—without taking reality into consideration—$21.5 billion in export revenues, but the collapse in the price of oil from $25 to $11 per barrel in the first five months of the year (and the perspective is that it will remain below $15 for at least the next several months) means a loss in income of approximately $7.5 billion. Therefore, Mexico will receive only $14 billion for its exports. But to keep its economy functioning even at the same level as last year—without any growth but also without any shrinkage—Mexico needs to import goods of a total worth of $13.5 billion. It is therefore clear that Mexico's export income will only just serve to cover the country's minimal income requirements. With the tiny trade surplus and what may be obtained from the services balance, Mexico will have a maximum of $2 billion at its disposal for servicing the foreign debt.

That is, the country's ability to service its debt (without strangling national production further) has been reduced to just $2 billion, which represents nearly 10% of the anticipated income from export of goods and services, and less than one-fourth of the $8.5 billion due in interest payments alone this year. This presumes a savings through lower interest rates, and does not take into consideration the principal payments on the debt which also come due this year.

If 25% of total exports of goods and services is allocated to pay the debt, then imports would have to be reduced by $3 billion, which means a 22% cutback over last year's levels. This would in turn lead to a contraction of approximately 5% in the gross national product for lack of sufficient resources to purchase abroad the raw materials and other goods required by Mexico's productive capability.

Thus, Mexico has no other option but to follow Peru's footsteps: break off negotiations with the IMF, set a ceiling on servicing the foreign debt *of no more than 10%* of export income, and reorient management of internal economic policy toward the genuine interests and priorities of the country. It is as simple as that. But to carry out such a plan requires a good dose of courage, intelligence, and patriotism to stand up to the consequences of such an action since, undoubtedly, affected interests both inside and outside Mexico will counterattack in hope of breaking the country.

Measures to be taken

From day one, a series of measures and decisive actions must be taken to manage economic policy, both internal and external. On the external front, Mexico must close ranks with other Ibero-American nations in order to strengthen its capacity of economic defense in conjunction with a strategically important sector of Ibero-America, including, above all, Brazil, Argentina, and Peru. This means arranging trade agreements to exchange oil and other Mexican products for food and manufactured goods from these countries. This is vital for the immediate future of the nation, since upon such actions depend the maintenance of certain vital aspects of trade, should certain of the industrialized countries with which Mexico trades allow themselves to be intimidated—either through weakness or stupidity—by the international banks, and launch economic reprisals against Mexico.

To eliminate the vulnerability of the Mexican economy as a result of its high level of dependence upon imports from the industrialized countries, Mexico would have to fully employ its negotiating talents on an international scale to counteract the effects of a possible trade blockade. The reality is that Mexico supplies numerous developed nations with a series of products crucial for the operation of their industries, products whose shortage could shut down certain productive sectors of those nations. Trade blockades can be made to boomerang against the perpetrators.

It is likely that threats of a trade blockade would remain threats, given the serious implications that such an action would have on the political and economic relations between Mexico and the aggressor country. But even in the event that some country might go beyond threats, Mexico's capacities of self-defense could prove far superior to what many people currently think. Further, one must remember that the most important chapters in the history of Mexico have been written under similar circumstances.

Let us look at the internal situation. The de la Madrid government would have to immediately take a series of measures that would assure it absolute control over monetary policy and public finances, reorienting them toward a strengthening of the productive apparatus and away from each and every one of the monetarist schemes which the current economic cabinet has applied either through the "recommendations" of the International Monetary Fund or through the obsession of certain cabinet members.

The first immediate measure to be ordered would be a lowering of international interest rates, both active and passive, which are currently approaching 120% and 90% respectively and which have become a principal factor in feeding the public deficit, in turn reinforcing inflation and corroding the resources of Mexico's productive sectors. Interest rates would have to be drastically lowered, at the same time that action would have to be taken on the national market to deactivate the inflationary motor through price controls and the imposition of exchange controls to halt flight capital.

At the present time, it is believed that certain government officials are putting the finishing details on a program known in the public domain as the "Aztec Plan," whose fundamental objective would be to stop the inflationary process cold by moving primarily against interest rates, prices, salaries, and the public deficit.

But for the Aztec Plan or any other program to function from the point of view of promoting economic development, more than measures to deactivate the inflationary process would be required. What is called for is another series of measures designed to reactivate the internal market and re-establish the nation's growth capacity. Such measures would have to guarantee the gradual recovery of consumers' purchasing power, of wages and of levels of investment in both the public and private sectors based on selective channeling of credit and public expenditure toward national priorities: economic growth, productive employment, and the population's welfare. No other plan will work.