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latter is a very large number, this restriction will be satisfied for realistic values of γ.

Given the restrictions in (A26)–(A28), it is easy to establish that the asset demands

$$D^w = h^w[Y^w(1 - \tau), r_d, \pi] \tag{A29}$$

$$C = g[Y^w(1 - \tau), r_d, \pi] \tag{A30}$$

have the properties

$$h_2^w, g_1 > 0, \quad g_3 < 0, \quad h_3^w, g_2 \gtrless 0.$$

The sign of h_1^w is positive or negative depending on whether

$$b_0\zeta_C - V_{EE}(r_d + \pi)[V_{DC} - V_{EC}(\rho - r_d) - V_E V_C \rho'] \gtrless 0. \tag{A31}$$

Casual observation and numerous empirical studies suggest that deposits are a normal, not an inferior, asset. Accordingly, I assume that the first positive term dominates the second negative term in (A31).

8 Debt Management and Negotiations

The Mexican debt began to grow rapidly in 1973 and is marked by three distinct phases. Table 8.1 presents a partial decomposition of the increase in the debt. What is striking in the decomposition is the fact that the net resource transfer accompanying the debt buildup has never been large. The resource transfer was greatest during the Echeverría administration, but due to large-scale capital flight in 1975 and 1976, the cumulative noninterest current account deficit totalled less than half of the increase in the debt. In the subsequent Lopez Portillo administration, the net resource transfer was negligible. Almost all new borrowing served to finance capital flight or interest payments on previously contracted debt; the cumulative noninterest current account deficit accounted for only 5 percent of the debt accumulated between 1977 and 1982. After 1982 the direction of resource flows was reversed and Mexico made large net transfers abroad. The De La Madrid administration ran the huge trade balance surpluses required to make interest payments on the debt. Unsettlingly, however, the current account registered a cumulative surplus of $9.6 billion from 1983 to 1986, even as the total debt

Table 8.1 Debt Decomposition (billion $)

	Current Account Deficit			
	(1) Interest[a]	(2) Noninterest	(3) Increase in Debt[b]	(2)/(3)
1971–76	6.00	8.81	20.07	.44
1977–82	31.63	3.52	67.26	.05
1983–86	34.98	-44.60	5.91	—

Sources: The decomposition of the current account deficit into its interest and noninterest components is calculated using data from *Indicadores Economicos* (Bank of Mexico). For reasons mentioned in chapter 4, Zedillo's figures (1987, 177) are used for the increase in the external debt.

[a]Private and public sector interest payments on the foreign debt plus remitted profits less income from Mexican investments abroad.

[b]Net increase in private and public sector foreign debt plus net foreign direct investment.

increased $5.9 billion. Part of the surplus reflected a substantial accumulation of reserves in 1983 and 1984, but much of it underwrote further capital flight.

In different periods, capital flight has been motivated by a heavily overvalued exchange rate. The absence of capital inflows after devaluation of the currency of realistic levels, however, indicates that the perceived relative return on domestic assets must have declined. This seems to reflect the operation of several factors. First, the return on domestic assets may be discounted by an "appropriation risk" factor; it is undoubtedly the case that part of the private sector fears the government may resort to drastic wealth levies (tax increases or partial wealth seizures, as with the Mexdollar accounts in 1982) to service the external debt. Second, real interest rates on bank deposits—the main saving instrument for the noncorporate private sector—were low or negative between 1973 and 1985. In 1986, high real deposit rates emerged. The high rates along with a severe reduction in private sector credit (forcing "distress borrowing") finally generated a small capital inflow, but 1987 brought renewed capital flight.

8.1 Institutions Relating to Debt Management: The Public Sector Debt

The branches of the Mexican government in charge of external debt policy are the Ministry of Finance (Secretaria de Hacienda y Credito Publico, or SHCP) and the Bank of Mexico. Within Hacienda, the Director General of Credit (DGC) has handled most issues relating to debt management. The DGC and the Bank of Mexico are responsible for formulating debt policy, authorizing new loans, keeping records on all loan transactions, and negotiating debt reschedulings.

One of the first steps taken by Lopez Portillo as president was to regulate the process by which foreign debt was contracted. On 31 December 1976, the General Law of Public Debt (Ley General de Deuda Publica) was

enacted. This law established the rules and regulations that were to govern the acquisition of foreign debt by the public sector. Hacienda was put in charge of contracting all debt for the federal government. Borrowing by the state-owned enterprises (SOEs) required prior approval by Hacienda. To obtain approval, the SOEs had to submit their budgets and investment plans to Hacienda. In addition to these responsibilities, Hacienda was assigned the task of collecting all information pertaining to the financial terms of the external debt (maturity, interest payments, amortization schedules, etc.). As a final control measure, the General Law stipulated that the yearly budget of the federal government include ceilings on external borrowing.

Although a large fraction of the foreign borrowing was done by SOEs (most notably PEMEX, NAFINSA [development bank], TELMEX [phone company], SIDERMEX [steel mills], and BANPESCA [fisheries bank]), Hacienda and the Bank of Mexico proved fairly adept at staying informed about the debt buildup. A comparison of the (now known) actual value of the public sector debt in 1980 and 1981 with the figures published by NAFINSA for those two years does not show large discrepancies (table 8.2).

In contrast to the public sector debt, little effort was made to keep track of the private sector foreign debt. Prior to 1983, the Mexican authorities did not require any type of registration of private sector debt (Gurria Treviño 1987, 24). The major problem in the debt management process, however, was not the lack of good information but rather the absence of a well-defined debt strategy. No single agency in the government had primary responsibility for monitoring the current account deficit and judging whether the pace of debt accumulation was excessive. The Ministries of Commerce, Finance, Planning, and Foreign Affairs all made separate estimates of the country's "capacity to pay." The various forecasts were usually in conflict. In the pivotal year 1981, Hacienda repeatedly warned that a softening in the world oil market was on the horizon. This counsel was emphatically rejected, and government policy was instead formulated on the basis of the more comforting forecast that the world market price of oil would average $55 per barrel for the second half of 1982.[1]

Nor did the foreign banks exercise much critical judgement. Regarded as a safe client because of its oil wealth, the Mexican government was long encouraged to borrow on the implicit understanding that its medium-term debts (three- to seven-year loans) would be automatically refinanced (Gurria

Table 8.2 **The Public and Publicly Guaranteed Long-Term Debt (billion $)**

Year	NAFINSA (1981)	World Bank (1985)
1980	36.9	38.9
1981	47.8	47.4

Sources: The World Bank and NAFINSA.

Trevino 1987, 13). Syndicated loans for numerous projects of extremely dubious merit, such as those that financed construction of the state-owned steel mills of SICARTSA, were often oversubscribed.[2] Even after mid-1981, when Mexico was clearly headed for trouble,[3] short-term credits could usually be arranged on the basis of just a promissory note or a tested telex (Gurria Treviño 1987, 14). In the general rush to lend, Mexican loans became a significant part of many banks' portfolios. Table 8.3 shows exposure as a percentage of primary capital in 1982 for eighteen U.S. banks. In several of the largest banks, exposure exceeded 50 percent. A large number of European (notably the Swiss Bank Corporation) and Japanese banks also participated in the lending spree and became heavily exposed.

Summing up, the changes instituted under the General Law of Public Debt did not improve control over external borrowing. The law may actually have contributed to Mexico's debt management problems insofar as foreign banks viewed Hacienda as guaranteeing repayment of their loans to the SOEs, regardless of the profitability of the projects financed by those loans.

8.2 The Debt Negotiations

A few months before the crisis became known to the world at large in August 1982, Jesus Silva Herzog, the Minister of Finance, commissioned a small task force to quantify the total debt of the public sector and to draw up a debt rescheduling proposal for submission to the country's creditors. In July, Silva started negotiations with the IMF in the hope of having a Fund agreement in hand before approaching the banks. The negotiations, however, did not progress quickly enough and, on 23 August 1982, Silva announced

Table 8.3 U.S. Bank Exposure, 1982 (% of primary capital)

Bank	%
Citibank	54.6
Bank of America	52.1
Chase Manhattan	40.0
Morgan Guarantee	34.8
Manufacturers Hanover	66.7
Chemical	60.0
Continental Illinois	32.4
Bankers Trust	46.2
First National Chicago	50.1
Security Pacific	31.2
Wells Fargo	51.0
Crocker National	51.2
First Interstate	63.0
Marine Midland	28.3
Mellon	41.1
Irving Trust	34.1
Bank of Boston	28.1
Interfirst Dallas	30.1

Source: Institute for International Finance (Washington, D.C.).

that Mexico would suspend all payments of principal for the next three months. In the days that followed, tense negotiations took place between the Mexican authorities and the banks under the auspices of the Federal Reserve.[4] The Mexican proposal to the banks called for

- Postponement of amortization payments until 31 December 1984 ($20 billion).
- $5 billion of new financing.
- All loans to carry an interest rate of 1.75 points over prime or 1.875 points over LIBOR.

The banks formed an advisory committee with William Rhodes of Citibank serving as chairman. On 15 December 1982, a rescheduling agreement was reached with more than 1,000 of the 1,400 banks involved in the negotiations. For the $20 billion of capital payments coming due between 23 August 1982 and 31 December 1984, the following terms were settled on (from SHCP):

- Rescheduling fee: 1 percent.
- Interest rates: 1.875 over prime or 1.75 over LIBOR.
- Maturity: Eight years with a four-year grace period.

For the new loan of $5 billion, the terms were:

- Fee: 1.25 percent.
- Interest rates: 2.125 over prime or 2.25 over LIBOR.
- Maturity: Six years with a three-year grace period.

The new $5 billion loan increased the participating banks' exposure approximately 7 percent. Each bank's contribution was determined by its share in total claims on the country as of August 1982. In exchange for keeping open the possibility of further reschedulings and for the four-year grace period given on the $20 billion of rescheduled debt, the banks obtained very high rates and commissions.

The impact of the 1982 restructuring on the amortization schedule for the public sector foreign debt is shown in table 8.4. The restructuring bought two years of relief, but at the price of a much more oppressive repayments schedule beginning in 1985.

The 1982 restructuring was followed in 1983 by new agreements more favorable to Mexico.[5] A $4.5 billion PEMEX acceptances facility was renewed in midyear for an additional two years. In December, the commercial banks agreed to make a new loan of $3.8 billion to the Mexican government. Again, individual bank participation was on the basis of pro rata exposure as of August 1982. The new loan carried far easier terms than the new money package of 1982. The interest rate was either 1.5 percent over LIBOR or 1.125 percent over the U.S. prime (at the election of the creditor), and the loan's maturity was set at ten years with a five-and-one-half-year grace period. Commitment and facility fees were also comparatively low.

Table 8.4 Profile of Capital Payments on the Public Sector Debt Before and After 1982 Rescheduling (billion $)

Year	Before	After
1982	8.14	.58
1983	8.96	1.47
1984	5.37	1.66
1985	9.67	10.17
1986	5.15	8.50
1987	7.53	13.73
1988	4.67	10.78
1989	3.52	9.13
1990	1.13	9.09
After 1990	3.16	5.33

Source: Notas Sobre la Reestructuracion de la Deuda Externa de México (SHCP).

The 1982 and 1983 agreements staved off an immediate crisis, but accomplished little more. Despite the reschedulings and the new money, Mexico made a large net transfer to its creditors in 1983 and 1984 of $14.7 billion.[6] Furthermore, adherence to the maturity schedule entailed a staggering $69 billion of repayments over the next five years (see table 8.6 below).

Confronted with a repayments schedule that presaged macroeconomic collapse, the Mexican authorities began to press for a more extensive, multiyear restructuring package. The banks' negotiating committee refused to discuss such a package for nearly six months and then in June 1984 allowed that it might be possible to reschedule payments coming due between 1985 and 1987. The Mexican team insisted that a longer term rescheduling was necessary, and after prolonged, intense negotiations, the restructuring package detailed in table 8.5 was agreed upon in the last quarter of 1984.[7] Five billion dollars of new money was provided, and all public sector payments on principal coming due between 31 December 1984 and 31 December 1989 were rescheduled to be paid over a period of fourteen years with a two-year grace period. Of the $43 billion of rescheduled debt, $23 billion had been rescheduled before, just after the 1982 crisis. The

Table 8.5 The 1984–85 Restructuring

$43 billion rescheduled ($20 billion not yet rescheduled and $23 billion previously rescheduled and coming due for payment):
Interest rates: .875 over LIBOR for the first two years;
1.125 over LIBOR for the next five years;
1.25 over LIBOR for the last seven years
Maturity: 14 years with a 2-year grace period
$5 billion of new financing:
Interest rates: 1.5 over LIBOR or 1.125 over prime
Maturity: 10 years with a 5-year grace period for $4 billion;
prepayment of $1 billion

interest rate on the restructured debt was cut roughly one percentage point, and LIBOR replaced the prime rate as the reference rate on most of the debt. Table 8.6 shows how the restructuring of both the commercial and official debt altered the profile of future capital payments. Over $40 billion coming due in the last half of the eighties was rescheduled to be paid between 1991 and 1998.

In addition to renegotiating the maturity and interest rate, the currency denomination of part of the debt was diversified. Non-U.S. banks were offered the option of converting a portion of their dollar debt into their own national currency. If 30 percent or less of the total debt was earmarked for redenomination, the conversion would be effected in equal monthly installments over a period of two years at the then prevailing exchange rate. For redenomination of 40 percent of the debt, the conversion period was thirty months, and for redenomination of 50 percent (the maximum allowed), it was lengthened to forty-two months. In all, $12.2 billion of the public sector debt was made eligible for redenomination. Table 8.7 indicates how the currency composition of the debt has changed since 1982. In practice, redenomination has been very limited. As of December 1985, dollar-denominated debt still claimed 90 percent of the total public sector external debt.

The catastrophic decline in world oil prices in early 1986 forced Mexico to seek new credit and a further restructuring of its debt. On 22 July 1986, the

Table 8.6 Profile of Capital Payments on the Public and Private Sector Debt Before and After 1984–85 Rescheduling (billion $)[a]

	Before			After		
Year	Total	Public	Private[b]	Total	Public	Private
1985	13.32	10.92	2.40	—	—	—
1986	10.83	9.43	1.40	7.66	4.95	2.71
1987	14.81	13.76	1.05	7.42	6.12	1.30
1988	15.71	12.48	3.23	6.57	3.38	3.19
1989	14.10	10.55	3.55	7.84	4.95	2.89
1990	11.04	8.46	2.58	8.05	5.51	2.54
1991	4.87	2.20	2.67	8.80	6.20	2.60
1992	2.65	1.87	.78	7.03	6.18	.85
1993	2.05	1.08	.97	7.18	6.25	.92
1994	.86	.69	.17	6.43	6.34	.09
1995	.45	.28	.14	6.49	6.13	.36
1996	.38	.25	.13	6.25	6.23	.02
1997	.26	.26	0	6.58	6.58	0
1998	.22	.22	0	6.48	6.48	0
After 1998	5.04	5.04	0	45.51	45.51	0

Source: Direccion General de Credito Publico.

[a]Repurchases of IMF debt are calculated under the assumption of full utilization of the Extended Fund Facility.

[b]Amortization schedule as of 31 December 1984.

Table 8.7 **Currency Composition of the Total Public Sector Debt (end-of-year, million $)**

Currency	1982	1983	1984	1985
Austrian Schillings	n.a.	26	18	22
Belgian Francs	n.a.	46	100	152
Canadian Dollars	n.a.	355	606	132
Deutsche Marks	1,561	1,412	1,170	1,416
Dutch Guilders	n.a.	124	119	162
ECUs	0	0	0	0
French Francs	n.a.	546	403	412
Italian Lire	n.a.	15	58	101
Japanese Yen	794	827	1,388	2,001
Pounds Sterling	1,002	1,007	659	921
Swiss Francs	690	480	475	640
U.S. Dollars	53,483	57,397	63,917	64,670

Source: Mexico Development Financing Strategy 1986, table 16 (SHCP).

Mexican government presented a Letter of Intent to the IMF, outlining the terms of an eighteen-month standby agreement, and approached the World Bank for a new loan. In August a $1.1 billion bridge loan was arranged with the Bank for International Settlements, eleven OECD countries, and the central banks of four Latin American countries.

The World Bank loan provided $2.3 billion in net financing to be disbursed over 1986–87. To qualify for the loan, Mexico agreed to continue the privatization of some state enterprises (those defined as "nonstrategic" by the government), to promote foreign investment, and to increase the scope of trade liberalization. All of these initiatives were inspired by the Baker Plan.[8]

Further in the spirit of the Baker Plan, the Mexican Letter of Intent called for new external finance to support structural reform and growth-oriented adjustment. The standby facility itself provided $1.4 billion in Special Drawing Rights to be doled out in seven installments between 1 November 1986 and 1 April 1988. The IMF approved the Mexican plan conditional on 90 percent of the commercial banks involved agreeing to participate. The banks, in turn, made their commitment conditional on Mexico's meeting the IMF's macroeconomic targets, the approval of certain World Bank loans, and the disbursement of a minimum amount of funds from the World Bank ($1.7 billion) and bilateral sources (Gurria Treviño 1987, 48–49). After more than four months of negotiations, on 20 March 1987 an agreement was finally struck with the banks entailing $6 billion of new money and rescheduling of $52.3 billion of existing debt (table 8.8).

The program also included three innovative contingency clauses. The first, with the IMF, provides an additional $600 million in the event that the world market price of oil drops below $9 per barrel. The other two contingency clauses are with the commercial banks and link a $500 million loan to the

Table 8.8 The 1986 Restructuring

A.	Debt contracted prior to 1982 ($43.7 billion): Rescheduled with a maturity of 20 years and a grace period of 7 years
B.	New loan ($6 billion): Maturity of 12 years with a 5-year grace period
C.	Debt contracted in 1983 and 1984 ($8.6 billion): Rescheduled with a maturity of 8 years and a grace period of 4 years
D.	Interest rates: U.S. Prime completely eliminated as a reference rate and all interest rates set at LIBOR plus .8125

economy's growth performance and a $1.2 billion loan for public investment to inadequate growth of export revenues.

In addition to restructuring the commercial bank debt, the Paris Club debt was rescheduled. All payments on principal coming due between 22 September 1986 and 31 March 1988 ($1.5 billion) and 60 percent of interest payments due between 22 September 1986 and 31 December 1987 ($282 million) were consolidated and scheduled for repayment over ten years. The new agreement includes a five-year grace period that effectively defers the first set of payments to 1 January 1992.[9]

The impact of the commercial bank and Paris Club debt restructurings on the total amortization schedule is shown in table 8.9. Capital payments for

Table 8.9 Profile of Capital Payments on the Public and Private Sector Debt Before and After the 1986 Rescheduling (billion $)[a]

	Before			After		
Year	Total	Public	Private	Total	Public	Private[b]
1986	7.66	4.95	2.71	3.61	2.07	1.54
1987	7.42	6.12	1.30	5.83	3.74	2.10
1988	6.57	3.38	3.19	6.48	3.30	3.19
1989	7.84	4.95	2.89	6.35	3.46	2.89
1990	8.05	5.51	2.54	7.33	4.79	2.54
1991	8.80	6.20	2.60	7.22	4.62	2.60
1992	7.03	6.18	.85	4.23	3.38	.85
1993	7.18	6.25	.92	3.87	2.95	.92
1994	6.43	6.34	.09	2.63	2.54	.09
1995	6.49	6.13	.36	2.01	1.65	.36
1996	6.25	6.23	.02	3.11	3.09	.02
1997	6.58	6.58	0	2.41	2.41	0
1998	6.48	6.48	0	3.06	3.06	0
After 1998	4.55	4.55	0	40.85	40.85	0

Source: Direccion General de Credito Publico.

[a]Repurchases of IMF debt are calculated under the assumption of full utilization of the Extended Fund Facility.

[b]Based on revised estimates of the private sector debt which reflect repayments made in 1985, Paris Club restructurings, and reclassification of data.

1986–89 have been lowered only $7.2 billion. Most of the adjustment comes in moving back payments originally due in the nineties. The new financing package lowers capital payments over the 1990–98 period by $27.4 billion.

Recently, the government has experimented with different mechanisms to reduce the debt burden. Since 1986, $2.3 billion of bank debt has been liquidated via debt-equity swaps. A debt securitization scheme (with the discount tied to the country's performance) proposed by Drexel, Burnham, and Lambert is also under consideration, but so far no move has been made in this direction.

8.3 Private Debt

Only a couple of the largest Mexican firms contracted credit directly with foreign lenders. Prior to 1982, most of the debt contracted by the private sector was arranged with banks which acted as intermediaries. A Mexican bank would obtain a loan from a foreign syndicate and then, under a different contract, lend the borrowed amount less a commission to some private company. The most important intermediaries were Nacional Financiera (NAFINSA) and the Banco Nacional de Comercio Exterior (BANCOMEXT) among the government banks (Banca de Desarrollo) and BANCOMER, BANAMEX, and COMERMEX among the privately owned banks. All of these banks had agencies in New York (and some in London and Tokyo) to tap the capital market. According to NAFINSA, some credits were arranged in less than an hour.

Firms were frequently used as a vehicle for capital flight. After obtaining a dollar-denominated loan, industrialists would deposit the loan proceeds abroad. This practice became widespread as the general expectation arose that the government would first devalue and then bail out firms with large dollar debts who faced severe liquidity problems.

Data on the private external debt are scarce and of poor quality. The World Bank figures seem to be underestimates since they frequently omit debt held with suppliers. The best data available, inaccurate as they are, come from the Bank of Mexico (table 8.10).

After nationalizing the private banks in September 1982, the government, in effect, held almost 100 percent of the private sector external debt. The de facto nationalization of the private debt occurred at the same time that massive devaluations created serious cash flow problems for many companies that were heavily indebted in dollars (i.e., those companies that were not merely a front for capital flight) but not exporting. To aid such firms, a financial scheme providing coverage of foreign exchange risk, FICORCA (Fideicomiso Para la Cobertura de Riesgo Cambiarios), was introduced. FICORCA is administered by the Bank of Mexico and works as follows:

- Any private company having dollar- (or any foreign currency) denominated debt can participate, provided it registers its debt with the Bank of Mexico

Table 8.10 **Private Sector Long-Term Debt (billion $)**

Year	Total	FICORCA	Paris Club	Other
1975	4.9	—	—	4.9
1976	5.5	—	—	5.5
1977	5.4	—	—	5.4
1978	5.5	—	—	5.5
1979	7.2	—	—	7.2
1980	11.0	—	—	11.0
1981	14.9	—	—	14.9
1982	20.0	—	—	20.0
1983	20.6	11.5	—	9.1
1984	18.8	11.9	.1	6.8
1985	17.6	11.0	.3	6.3
1986	17.0	10.6	.3	6.2

Source: Bank of Mexico.

- FICORCA grants a loan in pesos which is equal in value to the dollar amount the firm has borrowed. The participating firm gives its dollars to the Bank of Mexico, and the equivalent peso loan is calculated using the value of the controlled exchange rate on the day the company signs into FICORCA. FICORCA then services the debt on a quarterly basis only after the company makes its required payment in pesos to the Central Bank.
- The firm's peso payments are scheduled so as to be constant throughout the life of the contract (i.e., payments increase in nominal terms since inflation is high). Thus, in the first years of the contract, FICORCA grants a subsidy. In later years, payments exceed interest charges and the subsidy is recovered. As long as the domestic interest rate is maintained at its parity level (i.e., the foreign interest rate plus the percentage depreciation of the peso), the scheme has a net present value of zero.
- FICORCA does not involve the government in negotiating reschedulings of private sector debt. Each participating firm is responsible for renegotiating its own debt. To qualify for admission into FICORCA, the interest rate on the firm's debt must be LIBOR plus two points or lower and the maturity of the debt must be eight years and include a four-year grace period.
- FICORCA does not cover commercial risk. If a company goes bankrupt or for any reason falls behind schedule in its peso payments to FICORCA, the Bank of Mexico will not continue to service the company's dollar debt.
- Under the same conditions that apply to private sector firms, SIDERMEX (steel mills), BANPESCA (fisheries bank), and BANCOMEXT (foreign trade bank) can participate in FICORCA.

By October 1983 (the deadline for enrollment in the facility), FICORCA covered 1,121 firms holding 55 percent of the total private sector debt ($12 billion). The scheme has benefitted mostly large firms. Eighty percent of

FICORCA debt is held by 13.4 percent of the firms. The fifty largest firms alone account for 57 percent of the total debt.

The FICORCA facility probably prevented a chain of bankruptcies in 1982. The major risk is that the facility will become a fiscal drain. If the domestic interest rate drops below its parity level, FICORCA grants a permanent subsidy to the indebted companies. So far, this has not happened. Between April 1983 and April 1987, FICORCA generated net revenues for the government.

Two large, well-known Mexican companies, Alfa and Moctezuma, defaulted and withdrew from FICORCA until they could work out a restructuring agreement with their creditors. In both cases, the banks took some losses. The Alfa group's debt was $2.6 billion, of which $900 million belonged to the holding company while the remainder represented liabilities of HYLSA, its steel company. A steering committee was formed by Bank of America, Chase Manhattan, Citibank, and Morgan Guaranty. The restructuring of the holding company's debt involved a cash payment of $25 million, conversion of $200 million into peso-denominated debt, and a swap of the remaining debt for equity. Mexican shareholders have a priority right to acquire any stock the banks sell.

Moctezuma, one of the nation's largest breweries, obtained an even better deal. Its $307 million debt was rescheduled to be repaid over fourteen years with a six-year grace period. The interest rate on half of the debt ($154 million) is fixed at 3 percent, while for the other half the rate is LIBOR + 0.25 percent. Interest accumulated during the two years of negotiations was also forgiven.

9 Future Prospects: Is There A Way Out?

At the time of this writing (early 1988), prospects for the Mexican economy appear very dim. After achieving small but positive per capita growth in 1984 and 1985, the economy was sent reeling by the sharp drop in world market oil prices in 1986. The De La Madrid administration reacted to the oil shock by dispensing a stronger dose of austerity. Real fiscal spending was reduced slightly, and real credit to the private sector cut 9.6 percent. To limit the deterioration in the payments balance, the rate of depreciation of the peso was raised substantially, culminating in a huge 32 percent real devaluation by the end of the year. These policies, in conjunction with the fall in oil prices, resulted in triple-digit inflation (105.7 percent) and a decline in real