We would like to commend the staff for the candid and comprehensive assessment of the progress in implementing CAS for Mexico. We also would like to congratulate the Mexican authorities for a significant turnaround in their economy after the 1994/95 crisis. The progress achieved in growth, stabilization, structural adjustment, and even political reform, has been remarkable. Economy growth continues to be on a strong recovery path, exceeding the forecast in the last CAS by a wide margin. Current account deficit has been moderate. Inflation while somewhat high is well below the historical standard. Private capital inflow has rebounded significantly. In short, there has been very impressive performance on the macroeconomic front. Given the current crisis in East Asia, this CAS PR provides useful lessons, especially in identifying areas of difficulties in implementing financial rehabilitation and reform programs.

The impressive growth performance, however, masks some economic concerns that are well identified by the CAS PR, especially in the financial and energy sectors where some slippage has been experienced. Of particular concern is the banking sector where the recapitalization plan is plagued with uncertainty. However, due to substitution by cross-border lending, the liquidity conditions and credit system do not seem to be impaired by the continued weakness in banking sector. The CAS rightly pointed out that this trend cannot continue if the banking system is to play a positive role in development. Yet it is short on how to go about encouraging bank recapitalization apart form reform on the regulatory and supervisory side. While the regulatory and supervisory reforms are important and we encourage staff to push strongly for progress in these areas, they do not fully account for the inability to recapitalize. The experience on this front could serve as a good lesson for East Asia countries that are undergoing a similar exercise. I suspect in the case of Mexico that the cross border lending could partly explain the lack of investors’ interest in acquiring shares in these banks. Perhaps staff could comment on this.
We note the daunting challenges in the medium-term development fronts. The unemployment situation after the crisis has worsened poverty and inequality conditions. Yet the impact of the economic recovery is unevenly felt and further aggravates these conditions. Extreme poverty in rural areas is worrisome and the Government’s strategy to decentralize federal programs is a step in the right direction. We are pleased to note that the Bank is very much involved in this area and welcome the Annex providing more details on this aspect, which we find very useful.

Competitiveness is an issue which also deserves serious attention. Despite the remarkable progress on the liberalization front, Mexico has experienced poor productivity growth which has eroded its competitiveness. The strategy to open up the economy through NAFTA agreements and through its own unilateral efforts is the right one. We assume that these and other reform efforts would have a favorable impact on productivity growth through greater competition. This is not the case and given the projected moderate growth, the productivity growth is of crucial importance in the coming years. So far, we wonder whether the Bank really has enough understanding of the issue to develop the right strategy to tackle it. The CAS PR pointed out that the study on export competitiveness and labor market flexibility has just been completed. We wonder if staff can provide some preliminary findings, especially in identifying factors that are impediments to productivity growth as well as areas that need to be addressed. In this respect, we wonder how much our intervention in university education, which seems extensive, can help to improve the situation.

The progress on modernization of the state, which is one of the main themes of the CAS, is very short on details despite the fact that there was a long list of reform measures in the CAS. The reform in this area is of particular interest in many countries. Mexico’s experience could be very useful and perhaps staff could elaborate more on where the success was the greatest and where the progress has been slow.

Portfolio performance has been improving, reflecting better attention by staff and an improved economic environment. However, given the low disbursement ratio in 1997 and falling supervision resources, we encourage staff to pay adequate attention to this area.

Finally, the Mexican CAS was the first Joint CAS exercise. We wonder if staff can comment on the usefulness of this approach vis-à-vis the previous one.

Thank you.