We welcome the opportunity to discuss the proposal for a Country Assistance Strategy for Mexico and commend the staff for a thoughtful CAS. It is encouraging to see that Mexico has fared relatively well during the period of turmoil in financial markets and the collapse in international oil prices. Mexico also shows the most convincing signs of economic recovery in Latin America. The GDP growth in the first quarter was relatively high in a regional comparison. However, several development challenges remain.

We agree with the staff’s assessment that reforming the banking system is of high priority for the sustainable development of Mexico. This is a lesson also many other emerging market economies have learned during the past years of financial crises. But as Mr. Rivera points out in his written statement, this point is “barely supported by a Financial Technical Assistance Loan”.

There is also a need for further reform of the Mexican tax system. In particular, there is a need to strengthen the tax revenues. As experience from the Asian, Russian and Brazilian crises has shown, the most effective way for the emerging market economies to avoid contagion is to correct macroeconomic imbalances, overvalued exchange rates, structural weakness and strengthen the domestic financial sectors. It is therefore important to continue with the reforms. However, Mexico is entering a political period that will limit the room for reform. Although a comprehensive fiscal reform is needed, we can support the Bank’s more cautious approach to adjustment lending in the financial and fiscal sectors if sufficient reform progress is deemed lacking.

Even though inflation increased early this year, there does not seem to be any fear for a renewal of earlier inflationary tendencies. An important factor contributing to lower increases in prices has been the currency’s appreciation. The Bank assumes Mexico to reach the Central Bank's target of 13 percent for 1999. How would staff assess the risks for a return to higher inflation and how would such a scenario affect the base case lending?
Several important risks are mentioned in the CAS. An additional downside risk might be diminishing US demand. The CAS scenario is based on the assumption of continued expansion of exports. The risk of raised US interest rates or a correction in the US stock market should also be considered.

The biggest remaining challenge is poverty reduction in a situation with huge regional differences. Success in improving social services will be closely linked with progress made with decentralization. Among the most important areas, the quality of education remains a priority, and we particularly welcome the emphasis given to this area in the CAS. The government is, however, in a situation where limited fiscal resources impose a restraint. Alternative mechanisms should therefore be found to improve the human capital.

Finally, we welcome the efforts taken so far to deal with the environmental problems. There is a clear risk, though, that the high costs of Mexico's environmental degradation will before long increase even further.