Public Disclosure Authorized

THE WORLD BANK IN MEXICO: A CONTINUING PARTNERSHIP

Remarks

As Delivered

By

A.W. Clausen

President

World Bank and International Finance Corporation

before the

United States-Mexico Chamber of Commerce

Washington, D.C.

October 4, 1984

Thank you, Peter. Good afternoon, ladies and gentlemen.

The people in this room are making decisions that are vital to Mexico's economic future, and I'm delighted for this opportunity to take part in your discussions.

We have just ended very productive Annual Meetings of The World Bank and International Monetary Fund here in Washington, and you might be interested in a brief report on what happened there. I'd also like to bring you up to date on The World Bank's current involvement in Mexico.

* * *

We were gratified that the finance ministers and central bankers who spoke at the Annual Meetings were virtually unanimous in their support for The World Bank. They welcomed the innovations we've made over the last few years to help our member countries cope with the global recession. President Reagan honored us with a strong statement of appreciation for The World Bank and with a personal endorsement of our proposed action program for Sub-Saharan Africa.

One interesting aspect of last week's meetings was the U.S. Administration's announcement that they would welcome a new dialogue with the developing countries in the Interim and Development Committees. These Committees include representative finance ministers from the great majority of the world's nations, both industrial and developing nations. The ministers asked the IMF and World Bank to help them prepare for a meeting next spring. They will consider the broad topic of how to accelerate progress in the developing countries.

They agreed to discuss all aspects of the debt issue. We should now reach beyond the case-by-case restructuring approach that has worked so well in a period of crisis. We must discuss ways to secure growth. We will need to make full use of international institutions such as the IMF and World Bank, and we must also find ways to encourage an expansion of direct investment in the developing countries.

In view of the connections between debt and trade, the spring meeting of the Interim and Development Committees may be able to garner support for a new round of GATT negotiations. The World Bank has been urging the developing countries to join more fully in multilateral trade negotiations. We'd like to see the next GATT round focus on non-tariff barriers and on products of special concern to the developing countries.

So 1985 may well be a year of decisions that will shape the global economy for years to come. The first months of 1985 will probably be the best chance for the new Administration and Congress to forge agreement on how to get the U.S. fiscal deficit under control. Their success or failure will affect interest rates, the dollar, the U.S. trade deficit, and the continued strength of recovery around the world.

And the spring meeting of the Interim and Development Committees will give leaders of the industrial countries, including the new U.S. Administration, together with leaders from the developing countries a chance to move beyond the often fruitless confrontations of recent years. This new dialogue is a chance to settle on mutually agreeable action that will restore rapid growth in the developing countries and revive progress against poverty around the world.

In our meetings with Minister Silva Herzog and his colleagues last week, we again noted the foresight and firmness with which the Mexican Government has been implementing its stabilization program.

The World Bank has done some internal studies of Mexico's debt-servicing prospects, and the main conclusion that emerges is that Mexico can maintain growth in income and consumption from now on and solidify its creditworthiness again. What's crucial is continued improvement in Mexico's own economic management -- notably continued fiscal and monetary restraint and now vigorous action to remove disincentives for non-oil exports and for foreign investment. If the global economic environment is favorable -- that is, if the industrial countries continue their economic expansion and manage to roll back the tide of protectionism -- then, of course, Mexico's growth will be more rapid than it would be otherwise. But unlike some of the heavily indebted countries, Mexico should be able to make forward progress, economically and financially, even if the international environment is less favorable.

Mexico's experienced economic team has made great progress in reducing the country's fiscal and balance-of-payments deficits and in restoring the country's creditworthiness. Inflation hasn't come down as fast as expected (It's currently running at an annualized rate of about 40 percent), but Mexico's authorities seem determined to maintain fiscal and monetary restraint. Economic growth in Mexico is likely to be over two percent this year and probably around four percent in 1985.

We also noted Mexico's success in negotiating a long-term restructuring of its debt payments. The restructuring will feather out the bunching in Mexico's debt obligations. The country's creditors will be able to monitor its policies and performance, but the agreement will obviate the need for highly-publicized annual negotiations. So Mexico's economic team should now be able to turn their undivided attention to the tasks of reviving growth and of doing so in an equitable and politically sustainable way.

We expect oil prices to firm up again in the course of this decade, but not in the immediate future. And Mexico will need further investment in exploration just to keep oil production from falling.

So vigorous expansion of non-oil exports is essential. Mexico has already embarked on an export expansion program, and, together with the IMF, The World Bank is urging the authorities to move forward aggressively in rationalizing and relaxing foreign trade controls. These controls were designed to discourage imports, but they also discourage exports.

A revival of private investment, both domestic and foreign, is also of fundamental importance. Mexico's rapid growth in the Seventies was spurred by government spending, but burgeoning fiscal deficits led to financial crisis. Mexico would undermine its growing creditworthiness by resorting to deficit spending to reflate its economy now.

Many private investors are still waiting to see if Mexico's authorities will indeed stay on the path of economic reform. The irony, of course, is that continued hesitance on the part of private investors increases the risk of political resistance to the path of economic reform.

The investment climate surely seems more comfortable now that the government has managed to sell nearly all the non-financial assets of the nationalized banks back to the private sector.

And in our discussions last week, the Mexican authorities reiterated their eagerness to make conditions in Mexico more attractive to foreign direct investment. The government has some work to do to loosen up restrictions on foreign investment at the operational level, but the scope for investment is definitely widening.

Permit me to mention an issue of critical long-term concern to Mexico -- population. Mexico managed to bring its population growth rate down from 3.2 percent in 1970 to 2.4 percent today, and the Mexicans are continuing with their exceptionally successful population efforts. This is an area where still further progress is vital.

* * *

Now, let me tell you a bit about The World Bank's current program and plans in Mexico.

Mexico is important to The World Bank. For a long time, Mexico was the Bank's largest borrower, and even today Mexico accounts for over 7 percent of IBRD's outstanding loan portfolio, second only to Brazil. Our current activities include roads, ports, and railroads; both irrigation and dry-land agriculture; urban development, especially city water systems; vocational training; and credit programs for industry, for agriculture, and for mining.

As you know, The World Bank finances only part of any project, and Mexico, along with many other countries, has recently had difficulty financing its share of ongoing projects. We have responded with our Special Action Program. This Program involves increasing the share of World Bank financing and in other ways helping to maintain the momentum of high-priority, half-completed projects. The Special Action Program is working. Our disbursements to Mexico are expected to reach a record level in 1984 -- over $700 million.

Before the debt crisis, we had assumed that Mexico would "graduate" from The World Bank sometime in the 1980s. The debt crisis and global recession have substantially altered Mexico's economic prospects, and we are now in the process of building up a stronger pipeline of projects again. Mexican officials and Bank staff are developing new projects, appropriate for Mexico's present circumstances, in most of the sectors where The World Bank is already involved. We are discussing proposals for irrigation rehabilitation, agricultural extension and training, energy conservation, high technology development, low-cost housing, water pollution control, and solid waste disposal.

The Bank is also considering a power project, for the first time since the early Seventies. The World Bank stopped lending for power development, because it was considered politically impossible to raise tariffs to anything like economic levels. But Mexico's economic crisis has made the need for policy reforms of this type more obvious, and we want to support progress toward more realistic tariffs by investing in the sector again.

The World Bank is prepared to step up its level of new commitments to Mexico, if, in so doing, we can support more of the policy changes that are so urgently needed to foster growth. In 1983, for example, we committed a $350 million Export Development Loan to Mexico. This loan supported a package of reforms -- simpler administrative procedures for exporters, rationalized policies for export credit, and a relaxation of restrictions on certain imports.

There are pressing structural issues in other areas of the Mexican economy too -- in industry, in agriculture, in the social sectors -- and we have invited the Mexican authorities to propose further packages of policy reforms for which World Bank financing might be appropriate.

As you know, The World Bank has also been developing its potential as a catalyst for foreign investment. We continue to expand the International Finance Corporation. IFC is the World Bank affiliate which provides loans directly to commercial enterprises. IFC can also take equity positions in commercial enterprises.

Over the past two years, IFC has made investments in Mexican companies involved in agribusiness, petrochemicals, auto parts, cement, and paper. In planning future investments, IFC is emphasizing export projects and sectors in which Mexico has a natural comparative advantage.

We have also devised new modalities for commercial-bank cofinancing with The World Bank, our so-called "B-loans." In our fiscal year 1984, through June 30, cofinancing with The World Bank accounted for more than a tenth of all voluntary commercial-bank lending to the developing countries. The countries that have participated in the pilot phase of our B-loan program have managed to obtain longer maturities and better rates on the commercial loans involved. One cofinancing arrangement, in Paraguay, resulted in what amounts to a "cap" on Paraguay's future debt-servicing stream for the project, regardless of what happens to interest rates.

We haven't designed commercial-bank cofinancing into our projects in Mexico yet, but we hope the Mexicans will work with us on a cofinancing deal once their new debt restructuring agreement has been finalized.

* * *

The challenges still confronting Mexico are many and formidable. But there is no doubt about Mexico's rich potential, and the current authorities have certainly earned a vote of confidence. We at The World Bank are glad to be a partner in Mexico's future.

Peter Bottelier, chief of our Mexico division, is here with me today, and we will be glad to answer any questions.