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Washington, D.C.

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McNamara Papers

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Contacts with member countries: Mexico - Correspondence 02

Contracts  
Mexico (1972-1977)

Folder 2

RETURN TO ARCHIVES IN MC C3-120

ISN # 116327 ACC# A1993-012

BOX # 13

LOCATION N-473-1-2

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WBG Archives



## OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: June 5, 1972

FROM: E. Peter Wright *EPW*SUBJECT: Meeting of Mr. McNamara with the Secretary of Finance of Mexico,  
Mr. Hugo B. Margain

1. Mr. Hugo B. Margain, the Mexican Secretary of Finance, called on Mr. McNamara at 11:15 a.m. on Friday, June 2, after signing the loans for the Mexican railways and industrial equipment fund. He was accompanied by the Mexican Ambassador and by Mr. Julian Saenz Hinojosa, Counsellor in the Mexican Embassy, together with Mr. Rafael Isquerdo, Finance Secretary, Mr. Orive Alba, General Director of the Las Truchas Steel Company, and Mr. Adrian Lajous. Mr. Knapp and I also attended the meeting.
2. Mr. Margain handed over the attached list of projects which the Mexican Government would like to be considered for Bank financing in FY73, FY74 and FY75. Mr. McNamara welcomed the action that had been taken by the Mexican authorities to start building up a pipeline of projects and said that, while the Bank could not consider lending for everything in the list, his staff would be ready to review the list with the Government to see which were likely to be the most suitable projects for Bank financing.
3. Mr. Margain mentioned particularly the Las Truchas steel project and informed Mr. McNamara that a decree establishing a national steel policy committee along the lines suggested by the Bank had been approved by President Echeverria on the previous day. Mr. McNamara, observing that in several countries steel plants had been built for prestige reasons, emphasized the importance of steel being produced at costs that were internationally competitive and said that the Bank was only prepared to consider financing steel projects which met this criterion. Mr. Margain commented at some length on the achievements of the Mexican automobile and steel industries in developing exports of selected products.
4. Mr. Margain expressed particular interest in obtaining the Bank's support for agricultural development. Mr. McNamara, after referring to some of the problems encountered by the Bank-sponsored FAO mission to the Papaloapan area, mentioned the need for greatly strengthened agricultural extension and credit services in Mexico if the benefits of investment in agricultural credit and major irrigation projects were to be widely distributed.
5. Mr. Margain said that Mexico had to restrain the growth of its population and referred to the Government's new policy for "responsible paternity". Mr. McNamara welcomed this change of approach, but pointed

President has seen

June 5, 1972

out that it would take at least a generation for the results to make themselves felt. As another indication of the Mexican Government's concern to improve the condition of the people, Mr. Margain mentioned the new government housing fund, to be financed by a five percent payroll tax effective from May 1, 1972. This would have the task of building 100,000 workers' houses a year, with rents being limited to a maximum of 20 percent of a worker's wages. Mr. McNamara expressed an interest in learning more about this scheme and how it was to be financed.

Attachment

cc: Mr. Ljungh  
Mr. Knapp  
Mr. Gutierrez  
Mr. Nelson

EPWright:vr

## OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

DATE: June 1, 1972

FROM: E. Peter Wright *EPW*SUBJECT: Mexico: Visit of Secretary Margáin

1. After the loan signing at 11:00 a.m. on Friday morning, Mr. Margáin will probably want to talk to you about the present state of the Mexican economy and his hopes for future Bank lending. He is likely to be accompanied by Mr. Rafael Izquierdo, whom you know, and possibly also by Mr. Orive Alba, head of the Las Truchas steel company, with whom (and his British consultants) we are currently having extensive technical discussions here in Washington.

*ask about*

2. On the economy, Mr. Margáin may refer to the Government's concern over the apparently slow recovery of activity from last year's industrial recession and advance this as a reason for the President's hesitation in going ahead with the increases in power rates and other public enterprise tariffs which the Bank has long been pressing for. The Government does not have very good information about economic trends (this was one reason why they asked us to postpone this year's economic mission until the fall), but from what is known, it would appear that there have been delays in activating public investment, for which there was a large increase in this year's budget, and also that private investment continues to lag, probably reflecting in part the opposition of business groups to the present Government's mildly reformist tendencies. Exports on the other hand have been doing well, and the monetary authorities have probably been wise to maintain some restraints on credit expansion and not give too much of a stimulus to consumption.

3. So far as power rates are concerned, we have an understanding with the Mexicans that they will not take the steps needed for effectiveness of the next power loan (due for Board presentation on June 20) until tariffs have been raised on the average by 17-1/2 percent. The Loan Agreement also contains a covenant to the effect that the power sector will generate sufficient revenues to finance at least 18 percent of its investment in 1973 and 25 percent each year thereafter. The other issue which was causing us concern prior to the negotiation of the power loan has now been at least temporarily resolved by the enactment of a second decree on frequency unification, which opens the way for implementation of this long-delayed program.

→ 4. On the lending program, the Finance Secretariat has been preparing a plan for external borrowing to cover the period of the present Administration (to the end of 1976) and has drawn up a tentative list of projects for presentation to the Bank over the next few years. This is to be welcomed as a distinct advance over the past, when we have never had a meaningful pipeline of Mexican projects. However, we have considerable reservations about some of the Mexican proposals for Bank financing and also about the level of Bank lending they have in mind, which we have told them is quite unrealistic. (Their very preliminary lists add up to \$365 million for FY73, which would anyhow be impracticable on project grounds, \$475 million for FY74 and \$375 million for FY75.)

June 1, 1972

5. As we see the prospects for 1973, there are three or four loans aggregating rather over \$200 million which might be ready for Board presentation towards the end of the fiscal year as follows:

- low*
- (a) Another agricultural and livestock credit loan which could go up to \$100 million if we can find ways of extending it to reach some of the poorer farmers (but certainly not the very poor). We have a mission from the Agricultural Projects Department at present in Mexico working on this problem.
- (b) The Las Truchas steel project for which, in a recent letter to you, Nacional Financiera has requested \$75 million from the IBRD in combination with \$50 million from the IDB. We still have some serious reservations about this project, for which we do not yet have anything approaching firm cost estimates, and we are particularly concerned about the long delay on the Mexican side in setting up a national steel policy committee (along the lines of CONSIDER in Brazil) to formulate national steel policy and to prepare a long-term program for the overall expansion of the industry based on a careful study of the market. It would be helpful if you would remind Mr. Margáin that we reached agreement in principle with the Mexican Government last January on the establishment of this committee, but although the members of the committee have been selected (Mr. Margáin himself is one), it has not yet been formally established and nothing has been done to start building up the necessary technical staff.
- (c) Water supply for Mexico City. This could be anything from \$50-65 million and should be ready for appraisal in the fall, but it is a complex project with difficult institutional aspects, and we could have problems.
- (d) Another federal highway loan for \$20 million. This is not yet in our lending program, but could probably be appraised for Board presentation late in FY73 if we are satisfied that the package of roads proposed makes good economic sense (the principal item is a road to open up an undeveloped zone in the Zihuatanejo-Las Truchas region).

There is a fair chance that at least one of the four projects will slip, but we have a reasonable prospect of reaching a total for the fiscal year in the range of \$150-200 million. A project for agricultural and industrial secondary schools, identified by a recent Bank mission, could conceivably be squeezed into FY73, but this is rather unlikely. We have also had a mission working on the identification of a forest industries project, but there is still a lot of work to be done on this, and FY74 is probably the earliest that a loan could be considered.

6. In addition to the projects mentioned above, the Mexican project list for FY73 includes another \$100 million for major irrigation projects (including Papaloapan, on which we are already working) and \$20 million for

June 1, 1972

regional airports. We have promised to take a look at the airports, but even if the proposal makes sense, it is highly improbable that we could appraise it in time for Board presentation during the coming fiscal year. However, it is in the field of major irrigation and agricultural development that we run into the most serious problems, particularly in view of the Mexican suggestion that a further \$100 million of major irrigation investments should be included in the program for FY74. Quite apart from the question of timing, on which the Mexican ideas are totally unrealistic, we have reservations about continuing to put a lot of money into irrigation when the benefits are likely to accrue in large part to commercial farmers, as they have done in the past, while so little is being done to tackle the basic problem of rural poverty. This is also an issue with our agricultural credit operation.

7. There are, of course, very good reasons why so little is being done for the rural poor in Mexico and why it is extremely difficult for the Bank to find ways of helping them. Government agricultural services in Mexico (credit, extension, research, etc.), to the extent that they exist, have long been directed towards serving the better-off and more accessible sections of the farming community, and at the moment there are neither the institutions nor the trained people available to help in raising the production and income of the very poor. On top of this, there are a multiplicity of institutional obstacles that have to be overcome before investment in rural development can be expected to yield satisfactory economic returns (e.g. land tenure systems, forestry laws, local political bosses). As expected, we are running straight into all these problems in our attempt to develop a rural development project in the upper Papaloapan basin (linked with an irrigation project in the lower basin) on which a ten-man FAO mission has been working in the field during the past few weeks. Not only is there an almost complete absence of supporting agricultural services in the upper part of the basin, where many people are living close to the subsistence level, but the Papaloapan Commission, which is supposed to be responsible for the development of the water system, is heavily oriented towards major irrigation works (and the contracts that go with them), while displaying a minimal interest in the development of the poorer part of the region. In this particular case, moreover, it appears from the preliminary findings of the FAO mission that even the scheme to extend major irrigation in the lower part of the basin is poorly conceived and based on a quite inadequate study carried out by CIEPS, one of the best known Mexican consulting firms (founded, incidentally, by Mr. Orive Alba).

8. We are still some way from being able to suggest a meaningful strategy for the Bank to follow in attempting to deal with the problem of rural development in Mexico, but it is my view that we should not consider financing any more major irrigation projects unless we can first reach an understanding with the Mexican Government on the steps to be taken over the long term to overcome some of the major obstacles to improving the conditions of the rural poor. Obviously we cannot expect to see the whole political system reformed overnight, but there are some practical things which could be done, for example, to train more people at all levels for



June 1, 1972

work in rural credit and agricultural extension and to provide the incentives needed to keep them in the countryside. Hopefully, the national water study, on which we are working (with something short of enthusiastic support on the side of the Secretariat of Water Resources), will give us some leads as to what economic investments can be undertaken for the benefit of the not-too commercial farmers (e.g. tubewell irrigation in the central plateau). These are not questions which we are yet ready to discuss in detail with Mr. Margáin, but if the subject of agricultural development comes up at the meeting, you may like to bear these thoughts in mind.

9. Most of the remainder of the tentative Mexican proposals for Bank lending in FY73 through FY75 center on areas in which we are already involved, namely power, railways, roads, ports, tourism and industrial and agricultural credit. The Mexicans are, however, interested in obtaining a rising volume of funds from the Bank for education, with a second education loan of \$30 million included in their program for FY75.

cc: Messrs. Knapp, Chenery, Aldewereld, Chadenet, and Evans, Kuczynski, Nelson.

EPwright:vr



## OFFICE MEMORANDUM

TO: Memorandum for the Record

FROM: J. Burke Knapp

SUBJECT: Meeting with President Echeverria of Mexico

DATE: June 20, 1972

President Echeverria received Mr. McNamara, accompanied by Mr. Knapp, at Blair House on Thursday afternoon, June 15. The Mexican Foreign Minister, the Mexican Ambassador in Washington and Mr. Lajous were also present.

The meeting lasted for about half an hour and there were no new developments of consequence.

The President opened with a general exposition of the problems of economic development in Mexico, expressing warm thanks for the Bank's contribution to the financing of development projects there. It may be worth noting:

1. That in the second sentence of his remarks he referred to his Government's interest in the population problem; and
2. That he made scarcely any reference to the problems of agriculture and rural development, aside from a brief allusion to the Bank's support for agricultural credit.

In response, Mr. McNamara emphasized the Bank's interest in finding more effective ways to assist Mexico in rural development, and asked if the President had any suggestions to make in this regard. The President thereupon asked one of his aides to produce a handsome album presenting a Government program for the construction of feeder roads in Mexico's rural areas during the period 1973 - 1976. At the close of the meeting, Mr. Lajous was instructed to take this album and present it later to Mr. McNamara.

P.S. I understand from Mr. Lajous that this subsequent presentation will be accompanied by some sort of an application for a Bank loan to assist in financing this program.

cc: Mr. McNamara  
Mr. E.P. Wright

JBKnapp:vm

President has seen

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INTERNATIONAL BANK FOR  
RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL DEVELOPMENT  
ASSOCIATION

INTERNATIONAL FINANCE  
CORPORATION

OFFICE OF THE PRESIDENT

Mr. McNamara:

June 19, 1972

Visit of Mr. Victor Urquidi today at 6:30 p.m.

Mr. Urquidi is President of the College of Mexico, one of the few good schools of economics in Latin America, but seems to spend most of his time on other matters. A biographical summary is attached. He has been active on a number of UN committees. The last time you saw him was in 1969 when he asked for Bank support of a Latin American regional conference on Population (see attached note on that conversation).

At present Mr. Urquidi is acting as a consultant to the UN on the Application of Science and Technology. No doubt he will want to discuss with you the so-called World Plan of Action for the Application of Science and Technology to Development which is part of the strategy for the Second Development Decade. Within this plan a number of areas of research have been identified, among which are population and nutrition. The UN committee on the subject is presently working on regional plans for action. Mr. Yeganeh who is also a member of the committee will accompany Mr. Urquidi.

AL

*President has seen*

BIOGRAPHICAL SUMMARY ON VICTOR URQUIDI

Born in Neuilly, France - 1919

B. of Commerce - University of London - 1940

Economist with IBRD - 1947-49

Director Mexico and Central America Office of Economic Commission  
for Latin America - 1951-58

Economic Advisor, Ministry of Finance and Banco de Mexico, 1958-66

President Colegio de Mexico, 1966-to date.

Comment

Mr. Urquidi is one of the prominent Latin American Economists. As a senior advisor to Minister Ortiz Mena he worked closely and co-operatively with Bank staff. He has been actively promoting various types of research, including family planning, as president of the Colegio de Mexico, which is one of the outstanding universities in Latin America.

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## OFFICE MEMORANDUM

TO: MEMORANDUM FOR THE RECORD

DATE: October 4, 1972

FROM: Edgar Gutierrez

SUBJECT: MEXICO: Meeting with Mexican Delegation to Annual Meetings  
on September 25Present were: Bank

Mr. McNamara  
Mr. Knapp  
Mr. Alter  
Mr. Gutierrez

Delegation

10/13

Mr. Hugo B. Margain	- Minister of Finance
Mr. Ernesto Fernandez Hurtado	- Director General, Bank of Mexico
Mr. Miguel de la Madrid	- Director General Public Credit
Mr. Rafael Izquierdo	- Advisor, Finance Ministry
Mr. Alfredo Phillips	- Manager, Bank of Mexico
Mr. Adrian Lajous	- Executive Director

1. Mr. McNamara referred to the problem of generating additional public revenue, especially by raising tariffs of key government agencies, and asked about the Mexican plans for such increases. In response, Minister Margain summarized the difficulties produced by the 1971 recession and the compounded political effects of the fiscal measures initiated in 1971 to generate additional revenue and the steps which have been taken to improve tax administration, particularly by better techniques such as computerization. Fiscal revenues will jump about 6 billion pesos in 1971 as a result of the additional taxes and the reactivation of the economy. He pointed out that the fiscal effort was essentially geared towards a drop in the rate of external indebtedness of the country. He also covered a range of other topics relating to the economy, e.g. the good export performance which is occurring in 1972, rising foreign exchange reserves and the prospects for a 6.5 percent increase in real GDP in 1972. He presented a resume of the progress being made by President Echeverria in various fields, such as the creation of the workers' housing fund, a rural works program to help the peasants, and new credit regulations designed to assist ejidatarios and poor farmers. He also indicated that the Government is studying the tax measures to increase the burden on the rich relative to the poor.

2. Mr. McNamara then enquired again regarding the plans of the Government to increase tariffs in order to strengthen the very weak financial position of several decentralized agencies. In ensuing discussion Sec. Margain agreed on the importance of their having a sound financial base and then referred to Mexico's social problems and the need to avoid conflict. He also explained that Government officials concerned with fiscal policy

President has seen



October 4, 1972

favored the timely adjustment of tariffs but that those concerned with politics think differently, and that Government policy needs to consider both economic and political factors. During the discussion Mr. McNamara reiterated the importance of action on tariffs, particularly in the power sector. Minister Margain indicated that there was no doubt regarding the commitment reached with the Bank to increase power tariffs and the intention to take action accordingly, without specifying when this would be done. He said that he expected that action would be taken to increase Pemex prices before the end of the calendar year.

3. Mr. McNamara enquired as to the Government's attitude in the field of population, citing it as Mexico's number one problem. In response, Minister Margain indicated that population control was much more a question of paternity responsibility than of the availability of birth control techniques. Much, he said, could be done to improve channels for providing information on techniques for family planning. Plans are underway to do so through the Government clinics, which would represent a considerable change in Government policy. Mr. McNamara expressed his encouragement because of the visible change in attitude on this question in Mexican leaders. He also stated the view that work now being done in India relating to motivations, techniques and building institutions may well be useful in Mexico and pointed to the importance of prompt action relating to family planning in view of the long lead time that will be required to reach a position of stable "replacement" rates. Mr. Fernandez Hurtado referred to the need of taking advantage of modern advertising techniques to motivate the population of the country.

cc: Messrs: McNamara  
Knapp  
Chenery  
Lajous  
Kuczynski  
Lerdau  
Ruof (o/r)

RNelson/eg


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## OFFICE MEMORANDUM

TO: Memorandum for Record

DATE: December 18, 1972

FROM: Edgar Gutiérrez

*(for EG, E. Lora)* SUBJECT: Meeting of Mr. McNamara with the Minister of Foreign Relations  
of Mexico, Lic. Emilio O. Rabasa.

- 12/18
1. On December 11, at 1:30 PM. Mr. McNamara received the visit of the Minister of Foreign Relations of Mexico. He was accompanied by the Mexican Ambassador, Lic. J.J. Olloqui. Also present at the meeting were Mr. Knapp and myself.
  2. This meeting came rather as a surprise, since it was requested at a very short notice by the Ambassador. No special briefings were prepared in the absence of any indication about the purpose of the visit, other than a short one on immediate operational problems.
  3. Lic. Rabasa said that he had received a telephone call in New York from President Echeverria the previous evening, where Lic. Rabasa is attending the meetings of the U.N., to request him to extend a formal invitation to Mr. McNamara to visit Mexico next February. In addition, President Echeverria wanted to know the status and possible timing of the proposed loan for feeder roads, in view of the high priority that his Government wants to give to employment creating programs in the rural areas. (The President had presented to Mr. McNamara a volume for a program of 350,000 kilometers of feeder roads last June, during his visit to Washington).
  4. Mr. McNamara expressed his appreciation for President Echeverria's invitation to visit Mexico. He said that he has followed with great interest President Echeverria's statements on social reforms and in particular on the improvement of large masses of the rural population. However, he said that his travel plans for January and February were already firmed up and it would be very difficult to repeat a visit to a country before he had had a chance to visit other countries for the first time, responding to invitations already made.
  5. With reference to the feeder road program, Mr. McNamara indicated that we indeed have a road project in our FY 74 program, but it is entirely formed of primary and secondary roads, not feeder roads. The Bank had studied the package presented by the President in June and had found that the program was very much undefined in terms of priorities, costs and counterpart funds, requirements, and lacked economic analysis. It would therefore hardly constitute a project that could be included in our FY 73 and FY 74 operational

President has seen

Memorandum for Record

December 18, 1972

program. Much preparation work remains to be done to make of it a bankable project. Mr. McNamara referred to his letter of July 12, 1972 to President Echeverría on the issue of rural poverty, where special mention was made to the feeder road program and its still undefined scope.

6. Mr. McNamara expressed his disappointment with the still rather weak lending program to Mexico for FY 73 and FY 74. He said that the Bank was not yet doing in Mexico what it should in view of the severe problems of poverty in rural areas. He mentioned that other governments are receiving a much more valuable contribution from the Bank as a result of their own efforts to identify and prepare projects. The amount of work put now by the Mexicans in project preparation is disproportionately low with respect to rural needs of the country.

7. Mr. Knapp said that results in some of the big irrigation schemes have been disappointing and dubious from the point of view of their contribution to the solution of the problem of the poor. There is still a considerable lack of organization and coordination of the institutions involved in rural development.

8. Mr. McNamara indicated that the dynamic drive of the President had to be complemented by a more careful, detailed, procedural approach in project preparation and management. At one point he said that we have to finance "programs and projects", not "principles".

9. It was agreed that a detailed schedule for the preparation of the project will be worked out between the Bank and the Mexicans. A note on this matter will be sent by the Country Programs Department to Mr. McNamara, about a month from now, indicating the progress made and the reaction from the Mexican agencies to our suggestions.

Cleared with and cc: Mr. B. Knapp

cc: Messrs. G. Alter  
D. Knox/P. Geli  
E. Lerda

EGutiérrez:lc.

## OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara (through Mr. Knapp)      DATE: December 11, 1972

FROM: E. Gutierrez

SUBJECT: MEXICO - Visit of the Foreign Minister

- 12/11
1. Lic. Emilio O. Rabasa's request for a meeting with you comes as a surprise; we were not given prior notice and have no indication what is to be discussed.
  2. The most critical immediate issue between Mexico and the Bank at this time - but not one we would normally expect to be handled by the Foreign Minister - concerns Loan 834ME, the Fourth Power Sector Loan. As you know, the date of effectiveness is January 1 and a pre-condition was to be a 17.5 percent increase in power rates. This has not taken place and indications are that it will not take place but that the Bank will be asked to begin disbursing anyway. We have given the Mexicans no encouragement to expect that the Bank would acquiesce but have urged them to let us know promptly what their intentions are.
  3. I attach copy of a letter sent by Mr. Knapp to the Minister of Finance recently, as well as copy of a briefing memo to Mr. Knapp, listing the main bases of the Mexican commitments.
  4. Another issue which could conceivably come up is the Mexico City Water Supply Loan, where a tariff increase is a pre-condition for negotiation. Again, I would not normally expect this to be handled by the Foreign Minister, but just in case, I attach copy of a letter from me to the Minister of Hydraulic Resources on the subject. It has not been answered yet.

cc: Mr. Wiese  
Knox

ELerdau:jd

President has seen

## OFFICE MEMORANDUM

TO: Mr. J. Burke Knapp (through Mr. Gutierrez)

DATE: November 13, 1972

FROM: *clj* E. LerdaSUBJECT: MEXICO - Power Tariffs

1. You asked what the specific provisions of the Fourth Power Loan to CFE provided on tariffs. Loan Agreement Article 5.06 cross references to Article 3.03 of the Guarantee Agreement, which obliges the Government to

"... take such measures as shall be necessary, including but not limited to setting and maintaining or causing to be set and maintained rates for the sale of electricity (including the Power Consumption Tax) at such levels as shall be required, to provide the Power Sector with revenues sufficient to finance from net internal resources at least 18% of construction expenditures in 1973 and at least 25% in each year thereafter."

2. The grey cover appraisal report (PU-94a) links this objective to specific tariff increase:

"During negotiations it was agreed that the loan will not become effective until a tariff increase yielding at least 17.5% more revenue is introduced. The amount and timing are not yet definitive but the increase is to take place by the end of 1972. The covenant (of the Third Power Loan) requiring an 8% rate of return is to remain in force; however it was agreed that the sector will contribute, out of internal resources, at least 18% of the sector's investment in 1973 and 25% in subsequent years." (6.13)

3. The President's Report (P-1095) stated that

"... the procedural steps required in Mexico to initiate power tariff changes are now being taken ... Several months will be required to take all the steps needed to implement the rate changes, which the Government plans to bring into effect before the end of the year ..." (Para. 7)

"To avoid delay the Government has requested that the Bank proceed with the loan without waiting for the increase in power tariffs on the understanding that the documentation necessary for loan effectiveness will not be submitted until the tariffs have been raised. My recommendation is that we proceed on this basis; a letter from the borrowers and the guarantor incorporating the understanding would be signed simultaneously with the loan documents ..." (Para. 8)

4. A letter dated June 23, 1972, (the date of the Loan and Guarantee Agreements) signed by representatives of CFE and NAFIN states that

"... We hereby wish to confirm that we will not submit the evidence required to make the said Loan Agreement and said Guarantee Agreement effective under Sections 9.01 and 9.02 of the Loan Agreement and Sections 11.01 and 11.02 of the General Conditions unless average power rate increases of at least 17.5% are introduced in Mexico before December 31, 1972 ..."

Cleared with and cc: Mr. Cabezas

cc: Messrs. Alter  
Knox  
Sheehan

November 10, 1972

Lic. Hugo B. Margain  
Secretario  
Secretaría de Hacienda y Crédito Público  
Palacio Nacional  
México 1, D.F. Mexico

Dear Mr. Minister:

In accordance with the long tradition of close and effective collaboration between the Government of México and the World Bank, and following our past practice of frank and, I hope, mutually profitable exchanges of views on points of common interest, I should like to review with you some of the main issues, as I see them, in our present and planned operations in México.

Last year, as you know, our lending to México reached an all-time high (US\$277 million) and this year and the next we have similarly ambitious programs, all worked out in close consultation with you and your associates, as well as with the Ministry of the Presidency and other competent authorities. We have just sent to México a mission to appraise the Las Truchas steel project; another mission to appraise the fourth agricultural credit project is in the field; and a third appraisal mission is working on its report on the water supply project for the México City metropolitan area. If all these projects move on schedule, our new lending in the course of Fiscal Year 1973 might again amount to over US\$250 million. At the same time we are doing our utmost to respond to the Government's request to participate in irrigation projects; a mission to appraise a project in Sinaloa is scheduled to go to México this month; and arrangements to appraise the Pánuco project in the first-half of 1973 are well under way. These are just some of the activities that are envisaged or under way, and I mention them principally as an illustration of our expressed willingness to play an active and constructive role in México's development.

Such a role, however, is evidently predicated on a mutuality of objectives and on a common understanding of México's development needs and policies. In the past we have felt that such a consensus did, indeed, exist between us, and we have felt so all the more since President Echeverría's accession to office. His new initiatives on economic and social policies are very close to our own thinking, and it is the Bank's earnest desire to back these policies as vigorously as our staff and other resources permit.



We understand these new policies to consist primarily in devoting far more attention than was possible in the past to the least advantaged members of society. A strategy that combines México's past impressive performance on economic growth with an active attempt to spread the benefits of this growth increasingly widely seems to us eminently wise, and we wish to do whatever we can to support it.

You will, no doubt, agree, Mr. Minister, that an effective policy addressing the problems of México's poor - especially its rural poor - while at the same time not neglecting the investment needs of the modern sector of the economy, requires very sizable additional resources. Some of these can be obtained from abroad, and the World Bank stands ready to do its part once well designed programs and projects are presented to it. But the bulk of these resources will necessarily have to be mobilized in México and, given the nature of the case, this will mean in the public sector. Our recent economic mission has confirmed to us that the possibilities of freeing budgetary funds for such programs are limited and depend heavily on reducing the claims on the budget of the decentralized public enterprises such as CFE and PEMEX, especially as apparently no major new tax actions are contemplated.

I have mentioned the above to give you, Mr. Minister, a full background for the concern felt in the Bank when we were informed, recently, that a decision had been taken at the highest level in México not to raise electric power tariffs before December 31. You will recall, Mr. Minister, that there was a firm understanding between the Government and the Bank that our Power Program Loan No. 834 would not be made effective before the tariff increase had taken place. I refer, in particular, to your letter of April 4, 1972 ratifying this understanding, and to the conversation between you and Mr. McNamara at the time of the Annual Meeting in which the point was confirmed once more. I may add that we deliberated seriously among ourselves whether it would be better to postpone the signature of the loan - or even its presentation to our Executive Directors - until after the tariff increase had been put into effect, and that we finally decided not to do so because we felt confident that the Government's commitment to this action was definitive, and because we were anxious to offer our fullest cooperation to the Government and to CFE - one of our oldest and largest borrowers.

Our conviction that a tariff increase was vital, in view of the weakening financial prospects of CFE and of its large investment program, has not changed and has indeed been confirmed by subsequent developments. Nor, we gather, is there any disagreement on this matter at the technical level among CFE or Government staff. Moreover, it seems to us fully consistent with President Echeverria's social and economic policies to make the users of CFE - typically among the more affluent members of the community - pay a reasonable share of the cost of expansion of a sector that benefits them above all other segments of the community. This view is strengthened still further by the fact that the alterations in the tariff that had been proposed by CFE, while yielding a substantial overall increase in revenues, would have actually brought a reduction in the payments of the smallest - and presumably least wealthy - consumers.

I am informed that during his recent visit to México, Mr. Enrique Lerdaú, Chief of our México Division, discussed this problem both with His Excellency Minister Flores de la Peña and with Licenciado Lopez Portillo, of CFE, and that he urged both to present to the Bank, as soon as they considered it feasible, a statement of the Government's and CFE's intentions. I would like to take this opportunity to support this suggestion strongly, given the very serious consequences that further delays in the proposed tariff action would have for México, for CFE and for the Bank.

I gather that the whole issue is being reviewed by an Inter-Ministerial Group, in which your Ministry plays a key role. I also gather that there are good prospects that a high level delegation will, in fact, visit us in late November or early December. I sincerely hope that this visit will take place as soon as possible, and that the Delegation will bring to us proposals for action that will enable us to begin disbursements on the loan and to maintain our full program of activities in México.

In view of their obvious concern in this matter, I take the liberty of sending copies of this letter to Lic. Flores de la Peña and to Lic. Lopez Portillo

Yours very sincerely

J. Burke Knapp  
Senior Vice President - Operations

cc to: Lic. H. Flores de la Peña  
Secretario  
Secretaría del Patrimonio Nacional  
Insurgentes Sur No. 552  
México 1, D.F.

Lic. J. Lopez Portillo  
Director General  
Comision Federal de Electricidad  
Rodano No. 14  
México 5, D.F.

cc: Mr. McNamara  
Mr. Knapp  
Mr. Alter  
Mr. Gutierrez  
Messrs. Knox/Sheehan  
Messrs. Cancio/Cabezas

ELerdaú: 1d

November 9, 1972

Ing. Leandro Revirosa Wade  
Secretario de Recursos Hidráulicos  
Secretaría de Recursos Hidráulicos  
Pasos de la Reforma  
Mexico 1, D.F., Mexico

Dear Mr. Minister:

I am writing to thank you and your colleagues for the cooperation and courtesies extended to the recent Bank mission that visited Mexico to appraise the water supply project for Mexico City metropolitan area, and to inform you of some of its important findings.

I am happy to say that the mission has returned impressed with the project preparation and on the basis of their preliminary recommendations we are currently studying a Bank loan of about US\$75 million for the Comisión de Aguas del Valle de Mexico. In addition, we would be willing to study a loan for the water distribution systems of the Federal District and the State of Mexico should your Government be interested in such a loan.

The preliminary findings of the mission have raised two important issues on which I seek your views and, hopefully, your concurrence so that we can establish a common ground for further discussions and processing of the loan. These issues relate to (1) the Comisión's exclusive right to develop new water facilities in the valley, including the Pozos Sur and (2) measures for improving the water operations in the metropolitan area with a view to increasing revenues from consumers of water supply and sewerage services, reflecting the cost of these services more adequately in the tariffs, and adopting policies that are compatible with your urban planning and social equity objectives.

We are under the impression that a decision as to the agency that would develop the Pozos Sur project has not yet been taken. We understand that under Mexican law the Comisión has been given the exclusive right to build new water supply projects in the valley and we would be interested in getting your confirmation that the Comisión will be developing the Pozos Sur project as well.

Attached is a summary of information available to us concerning the water supply sector, present and future, in the metropolitan area. This information, which may lack precision, but is, we believe, correct in orders of magnitude, highlights the water supply dilemma faced in Mexico City. We believe financially strong institutions and a revised water tariff policy are essential for the effective resolution of the problems facing the sector.

At present, retail water tariffs in the Federal District, which have not been increased since the early 1950's, yield revenues which meet about 30 percent of the costs of providing the service. Decentralized agencies (such as PEMEX) which themselves sell products to consumers, obtain water free, and the resulting shortfall in water revenues are made up from the general revenues of the Federal District. Consumers residing outside of the Federal District - and the majority of low-income consumers reside there - pay considerably more for water than those within the District. Finally, the relatively cheap water in the Federal District is an incentive for water consuming industries to be located there, and for residential consumers to use water wastefully.

The seriousness of the problem is compounded because future water supplies are becoming more costly. The cost of bulk water from the schemes to be built in the years 1973-76 is estimated to be at least Mex\$0.95 per cubic meter, and will increase to Mex\$1.40 - Mex\$2.00 (at 1972 prices) from projects to be put up in the period 1982-87. Given the certainty of steeply rising real costs of bringing additional water to the metropolitan region - especially after 1980 - and given the unmet ability of large segments of the Federal District's water users to pay, it is considered vital to bring prices into a more rational relation to incremental costs.

In view of the above we would wish to suggest the following:

- (i) a 100 percent increase in revenues from retail consumer charges in the Federal District, as recommended by a recent tariff study;
- (ii) agreement that retail water and sewerage revenues would cover the costs of providing the services;

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1/ Costs are defined in the annex, footnote 1.

2/ The proposed tariff boost would substantially eliminate subsidies from outside the sector, and could partially be achieved by eliminating free water to decentralized agencies and by improving metering, billing and collection procedures and policies.

November 9, 1972

- (iii) development of a tariff structure which favors the very low-income consumer group by providing minimum water needs at a price they can afford, with the revenue short-fall, if any, made up from: (a) increased property taxes and/or (b) water sales revenues from larger consumers through a progressive tariff structure.

We propose that a study be undertaken immediately to establish the means for accomplishing (ii) and (iii) above, or that we be given the opportunity to review the existing studies with you and, if the recommendations would accomplish the above, these be adopted.

If you agree with the above principles, there would be several ways of ensuring these. As examples we enumerate some alternatives below:

- (i) an arrangement by which the Federal District and the other major retailers would become a party to the loan agreement with our Bank;
- (ii) an arrangement with Hacienda and/or Presidencia guaranteeing tariff performance by the Federal District and guaranteeing to arrange with the Federal District a data collection system that would permit cost and tariff monitoring; access to these data to the Bank would also be guaranteed by the Federal Government;
- (iii) a commitment by the Federal Government to maintain retail tariffs in proportion (to be established) of bulk rates; the latter would be established so as to achieve specific financial objectives for the Comisión.

We would be interested in your reactions to the above and would be equally open to review with you any other proposals that in your view would achieve the main objectives. One of my staff members will be visiting Mexico in early December and would call on you to understand your Government's views.

I am taking the liberty of sending a copy of this letter to Lic. Hugo B. Margán.

With best regards,

Yours sincerely,

Edgar Gutiérrez  
Program Director  
Latin America and the Caribbean

Attachment.

cc: Lic. Hugo B. Margán

Secretario Hacienda y Crédito Público

Cleared with and cc: Messrs. Lerdau, Bruestle  
cc: Messrs. Sheehan, Kalhermatten, Clyde

DDutt:mgf

MEXICO CITY: WATER SUPPLY DATA

	<u>1972/73</u>	<u>1975</u>	<u>1980</u>	<u>1985</u>
1. Population metropolitan area (million)	10.5	12.0	15.5	18.5
2. Water demand metropolitan area (m <sup>3</sup> /sec.)	42	49	65	77
3. Natural replenishment in valley (m <sup>3</sup> /sec.)	33	33	33	33
4. The average cost <sup>1/</sup> of water sold in Federal District (Mex\$/m <sup>3</sup> ) (at 1972 prices)	0.90	0.90	0.94	1.60 - 2.20
5. Revenues per m <sup>3</sup> sold in Federal District (Mex\$/m <sup>3</sup> ) (1971)	0.27	?	?	?

Supply m<sup>3</sup>/sec. metropolitan area

Existing Systems

DF sources	6. Natural replenishment	26	26	26	14 <sup>2/</sup>
	7. Mining of ground water	6	6	6	0 <sup>3/</sup>
8. State of Mexico sources		10	10	10	10

New Systems

In valley	9. Natural replenishment	0	2	15.5	15.5
	10. Mining of ground water	0	8.5	8.5	8.5
11. Outside valley		0	0	0	29 <sup>4/</sup>

Note: At present, retail water supply tariffs in the District yield only Mex\$0.27 per cubic meter and there is no sewerage tariff. Water supply operation, maintenance and depreciation costs are about Mex\$0.40. If a rate of return were earned, the cost would be about Mex\$0.90. The inclusion of sewerage costs, which may approach the level of water costs, could increase the costs to Mex\$1.50 or more.

Sources:

1. ATEC Engineering Consultants
2. ATEC Engineering Consultants
3. IPESA and Federico Mooser (Consultants)
4. Computed from ATEC Figures
5. Computed from ATEC Figures
- 6 - 11. ATEC Engineering Consultants

Footnotes

- 1/ The cost of water includes all operating costs, depreciation (estimated by ATEC) and a 10 percent return on the net value of the Federal District's bulk water and distribution assets. The fact that an increasing proportion of the bulk water for the Federal District will be supplied by the Comisión has been taken into account. The cost of the bulk water from the Comisión includes operating costs and a capital recovery factor based on the investment costs in current prices (10 percent interest, 30 years pay-back period). Operating and capital costs of sewerage facilities in the Federal District are not included. These figures will require to be further revised upwards for the annual inflation.
- 2/ It is assumed that the Lerma source will be returned to the State of Mexico by 1985 for the supply of the Valley of Toluca.
- 3/ It is assumed that overexploitation in Mexico City proper is ended by 1985.
- 4/ This volume could be reduced or eliminated by increasing the quantity of overexploitation in the valley.

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## OFFICE MEMORANDUM

TO: Memorandum for the Record

DATE: March 2, 1973

FROM: Gerald Alter *GA*SUBJECT: Meeting of Mr. McNamara with the Ambassador of Mexico,  
Mr. José Juan de Olloqui

1. The Mexican Ambassador, Mr. José Juan de Olloqui, visited Mr. McNamara on March 31. Mr. Alter was also present. The Ambassador extended, on behalf of the President of Mexico, an invitation to Mr. McNamara to visit Mexico in the near future, preferably prior to the President's departure on a trip at the end of March to Moscow, Peking, etc. The Ambassador emphasized that Mr. McNamara could make a very significant contribution to Mexico's development, if he were to visit at this time. The President is re-thinking many questions of policy and he had a very open mind on many important policy issues.
2. Mr. McNamara explained his general policy of limiting his visits to those less developed countries that he had not visited before. At the urging of the Ambassador, he agreed to consider the request. Mr. McNamara said that he would hope to give a reply before Wednesday, March 7, but the Ambassador suggested that if it was going to be in the negative, he would prefer that the decision be postponed.
3. The Ambassador stated that he understood the Mexican request for Bank assistance in the financing of feeder roads was at an advanced stage of consideration within the Bank. Mr. McNamara explained that a mission had just returned from Mexico. While we were very much impressed with the speed with which the feeder road program was being executed, we did not feel that, as presently conceived, it was very attractive as a project for Bank financing. While we would have been prepared to consider a feeder road program whose longer term benefits in terms of increased agricultural output could be identified, the program now being executed was put forward only as an employment creation activity during the construction period. The Ministry of Public Works had made no examination to establish agricultural benefits. Thus, we had been more attracted to the integrated rural development approach now being pursued by a joint Hacienda-Presidencia team. We were now considering in the Bank how we might assist in preparing a series of integrated rural development projects in selected regions. It was called to the attention of the Ambassador that the Mexican authorities needed to sort out the institutional arrangements for the planning and execution of the rural development program.
4. The Ambassador reacted with full understanding of the Bank's position, implying that he personally also had great doubts about the feeder road program and expressing a clear preference himself for the approach giving greater emphasis to the longer term production effects.

President has seen

March 2, 1973

5. After the meeting, the Ambassador said to Mr. Alter that he felt one of the advantages of a visit by Mr. McNamara to Mexico would be the opportunity it would give to obtain the President's full support for a rural development program.

cc: Mr. Knapp, Senior Vice President, Operations  
Mr. Gutiérrez, Director, LAC 1  
Mr. Knox, Director, LAC Projects  
Mr. Yudelman, Senior Adviser, Agriculture Department  
Mr. Lerdau, Division Chief, LAC 1  
Mr. Goffin, Division Chief, LAC Projects

GAlter:pa.

## OFFICE MEMORANDUM

TO: Mr. Robert S. McNamara

FROM: Gerald Alter *ga*

SUBJECT: MEXICO: Your Meeting with the Mexican Ambassador at 6:00 p.m.  
on Thursday, March 1.

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DATE: February 23, 1973

1. Dr. José Juan de Olloqui, Ambassador of Mexico to U.S.A., is calling on you on Thursday, March 1. Presumably he would be following up on the invitation the Foreign Minister (Dr. Emilio O. Rabasa) extended to you on December 11 to visit Mexico and personally observe the rural development - especially the feeder road - program of the Government. He may also seek Bank assistance for the program.

2. Recently a Bank mission, consisting of Messrs. Yudelman, Lerdau and Goffin visited Mexico to observe the Mexican initiatives in addressing the problem of rural poverty. They have just returned, and their back-to-office report is attached. During its meeting with Mr. Bracamontes, the Minister for Public Works (SOP), the mission learned that the Minister was under the mistaken impression that you would be visiting Mexico in March 1973. When the mission corrected this misapprehension, the Ambassador was instructed to call on you again and repeat the invitation. Apparently the Government is under the impression that your visit will expedite Bank involvement in the Mexican rural development program. As you will see from the attached report, the mission has made a positive recommendation for Bank support though, at the same time, it has drawn attention to (a) existing inter-ministerial rivalries within Mexico regarding jurisdiction over the rural development program and access to the funds, and (b) several conceptual and institutional shortcomings of the program. I would suggest that you refer to your prior engagements and avoid any commitment for visiting Mexico at this stage.

3. After discussing the back-to-office report of Yudelman et al with Mr. Baum and my other colleagues I shall make a recommendation to you on what action we should take to assist Mexico with preparation of a rural development project suitable for Bank financing.

Attachment.

cc: Messrs. Knapp, Senior Vice President, Operations  
Baum, Vice President, Projects  
Gutiérrez, Director, LAC I  
Knox, Director, LAC Projects  
Yudelman, Senior Adviser, Agriculture Department  
Goffin, Division Chief, LAC Projects  
Lerdau, Division Chief, LAC I

DDutt:mgf

President has seen

## OFFICE MEMORANDUM

TO: FILES

FROM: M. Yudelman, P. Goffin, E. Lerdau and D. Dutt

SUBJECT: MEXICO: Rural Development Programs

DATE: February 23, 1973

Introduction

1. This memo records our impressions of a visit made February 5-13 (5-10 in the case of Yudelman and Goffin), to obtain a clearer view of various recent Mexican initiatives in addressing the problem of rural poverty.
2. Mexico is faced with tremendous pressure to improve social conditions through increasing employment opportunities and reducing income disparities and mass poverty in rural areas. President Echeverría, even before he assumed office for a six-year term on December 1, 1970, expressed deep concern for the rural poor; and his election pledges included a commitment for reduction of rural unemployment, poverty and ensuring social and economic justice to peasants who had been bypassed while the economy grew. The present Government has accordingly taken several steps to alleviate rural poverty, which inter alia include (a) adoption of legislative measures - like the new Agrarian Law (1970), the new Water Law (1972) directed to achieve a more egalitarian rural society, (b) direction to financial institutions to earmark part of their resources for credit to small farmers and ejidatarios, (c) launching an employment creating rural roads program, and most recently (d) initiating an integrated rural development program.
3. The two last mentioned programs as presently envisaged are to cost about Mex\$15 billion (US\$1,200 million) in four years 1972-1976 and the Government has requested Bank assistance. At present these two programs are competing for funds, and the approaches to the Bank reflect this competition. In spite of the difficulties - institutional as well as of programming - that we foresee, we recommend that the Bank become involved in one of these programs, initially providing two or three staff members to work with the Government for a period of 2-3 months to assist in formulating a more effective program. The Mexican Government is going ahead with investment in infrastructure and Bank involvement may bring out a desirable change in strategy, whereby the "integrated rural development" program can be made more production-oriented than at present.
4. While making our recommendation for Bank involvement we wish to record three caveats.
  - a. The Mexican institutional structure in this field is so weak and authority and responsibility are so ill defined, that Bank involvement is necessarily a high-risk venture.

- b. Project preparation, appraisal and supervision will all be larger claimants on Bank staff (and consultants) time than are conventional projects; if the Bank cannot provide these inputs, it would be better to eschew involvement in this kind of project.
- c. We think the Mexicans should press on with (improved) programs of the kind described below, and that the Bank should be involved. With a total population of about 50 million of which about 20 million are close to subsistence and in rural areas, growing at 3.5 percent per year, we believe that these activities will merely provide an interim solution, a breathing space of between 10 and 20 years, and that ultimately the development of the country must be along other lines. There are still untapped productive potentials in Mexican agriculture, and programs of the kind considered here can help exploit this potential and raise rural incomes, often quite appreciably. In the medium term irrigation and drainage projects and colonization projects in the south will also provide partial solution and relief, but the resource base in many densely populated parts of rural Mexico is too poor to provide a decent livelihood for the masses of people living there - now or in the future - and longer-term solutions will have to involve broad-based decentralized industrial development, population shifts and, most importantly, a reduction in the population's growth.

5. During his meeting with President Echeverría on June 15, 1972, Mr. McNamara expressed the Bank's interest in finding more effective ways to assist Mexico in rural development and asked if the President had any suggestions to make in this regard. In response a "labor-intensive feeder road program" was presented to the Bank in June 1972. In November the Government formally requested a Bank loan for a \$400 million "investment program for the rural sector" and the Foreign Minister of Mexico called on Mr. McNamara on December 11 reiterating Government's interest in Bank support for the rural roads program. However, the Ministry of Finance has advised the Bank since that the Government is essentially interested in Bank support for an integrated rural development program, of which the roads would be one of the several components. Thus, at the time our mission reviewed possible rural development programs with the Government there were two rival claimants for funds: (i) the Ministry of Public Works (SOP) which has in the meantime diversified its employment creating, Keynesian, investment program so that it includes other works like small dams and water reservoirs, soil conservation, school buildings and even some small-scale industries, besides feeder roads, and (ii) the Ministry of the Presidency - Finance Ministry sponsored "integrated rural development program" consisting of a comprehensive works program including some production components organized in specified regions, each covering

about 10,000 square kilometers and rural population ranging from 30,000 to 120,000. While it would eventually be for the Mexicans to decide which Ministry would coordinate and execute the rural development program, we think that early resolution of this issue would facilitate Bank involvement in the program.

Observations in Mexico

6. The total Government investment program in Mexico for 1973 is about Mex\$16 billion (Mex\$1 billion equals US\$80 million) of which Mex\$4.5 billion are earmarked for "rural development". Of the latter, Mex\$2.5 billion is for new programs, of which Mex\$1.2 billion have already been allocated, as follows:

	<u>Mex\$ million</u>
Five integrated rural development regions (Presidencia - Hacienda Program)	232.0
Rural roads (SOP)	695.0
Small irrigation	175.0
Miscellaneous	<u>133.0</u>
	<u>1,235.0</u>

The first item in the above Table is an innovation and attempts concentrated development of economic and social infrastructure in selected areas. The Presidencia and the Ministry of Finance expect this program to gather momentum in the coming months and eventually to absorb the other single discipline programs. The Bank was invited by them to participate in this integrated program.

7. The SOP (Public Works) Program: The Minister of Public Works, Mr. Bracamontes, is a dynamic personality, an excellent organizer, and was the first in the field with a proposed four-year program of 350,000 kilometers of labor-intensive feeder roads requiring an outlay of about Mex\$13 billion. Of the rural development funds so far allocated, the SOP has got the major share (Mex\$695 million out of the 1,235 million plus the rural roads component in the integrated program) and its program provided employment, at the minimum wage level, to 200,000 people in 1972; currently to 250,000 and would increase to 300,000 a day (involving a daily expenditure of about US\$0.5 million) by the end of the year. These roads cost about Mex\$50,000 (US\$4,000) per kilometer, 80 percent of which is spent on wages. The program is being diversified, covering other works of village interest (minor irrigation, schools, etc.) and university students are being invited to work in the program on the Peace

Corps analogy. The Minister stated that his agency covers the entire country and has the administrative ability to execute a comprehensive rural development program.

8. The Hacienda - Presidencia Program started only recently and covers five regions with a 1973 budget of Mex\$232 million (US\$18.6 million). Teams of experts make a survey of selected regions and prepare four-year development programs covering activities such as construction of roads, small irrigation, soil conservation, provision of education, health, housing, marketing and rural electrification in the area. In some cases they also have developed production programs for the region, and included livestock, forestry and fruit-trees among the investments to be financed. It is alleged that on average it has taken two weeks for the group to prepare each regional program and at the time of our review, in addition to the five active regions, programs were said to be near completion for eleven more regions and the Government expected to have 40 integrated development regions by the end of the year. The stated objective of the program is to generate additional production in the region and the creation of lasting employment opportunities to absorb the labor employed in the construction phase of the program but this notion does not yet seem to have permeated fully to working levels.

9. The integrated rural development program is directed by an inter-ministerial committee under the chairmanship of Mr. Hiriart (Director of Public Investments in the Presidencia). The Presidencia also has a small Secretariat which attempts to coordinate the detailed programs prepared in the various ministries affecting the selected region. There are committees at the state level, presided over by the State Governors, including state level staff of the concerned ministries. Associations of beneficiaries would be developed at the regional levels to look after the post-construction aspects of the program - namely, maintenance, operations, etc. At the time of our visit the institutions at the state and regional levels were in the formative stage.

#### Mission Impressions

10. Despite the dynamic personality of the Minister of Public Works and the impressive record of action of his Ministry, we do not think that his feeder road program per se would make any lasting impact on the rural economy. As long as it lasts the wages are welcome, but the rural communities have only a limited capacity to benefit economically from most of the roads and these are not necessarily the priority needs. The inflationary pressures of the wages in the present imperfect market organization in the rural areas could syphon off the wage earnings into undue profits of the local merchants. The post-construction contraction in employment opportunities in the locality could lead to nightmarish problems. Accordingly, the mission was very candid in saying to all the government agencies - including the SOP - that it would not recommend Bank assistance to the feeder roads program as presently constituted.

11. The program is impressive primarily in the speed with which people were put to work and, in the drought of 1971/72, clearly produced some good. But it is not primarily development-oriented; however useful the individual works may be - a few classrooms or a health post here, some soil conservation or a rural road there - the quality of life in the villages where they take place will be essentially unaltered, the opportunities for gainful employment after the works are finished will not have expanded significantly and the lasting impact of the program will be negligible. We have some reason to believe that concerns of this kind have also appeared in the Ministry of the Presidency, but, given the President's urgent desire to do something, it seems clear that the SOP program will continue or expand at least until it can be replaced by something that is not only demonstrably better in design but that also meets the standards of operational effectiveness set by SOP. In short, it will have to be a program that not only is development-oriented but that also is capable of moving the various institutions whose responsibilities and jurisdictions are involved, to subordinate their activities to a single design suitably administered and to spend their funds in such a way that they mutually enhance each other's effectiveness. SOP operates on a large scale; it remains to be seen whether its competitors can do likewise.

12. The so-called Integrated (Presidencia - Hacienda) Program does not yet meet this standard, even though conceptually it seems to us to be more promising as a development program than the SOP program. Although it is also heavily infrastructure-oriented in its approach, it recognizes that the production aspect should be an integral part of the program and play a more important role. Institutionally and organizationally it still seems weak. The coordinating committees, in our view, cannot be a substitute for sound administrative organizations, even less so in Mexico where both the Presidencia and the Finance Ministry presently play only a limited role in curbing the programs and wishes of individual ministries. Moreover, the strength, organization and coverage of the ministries and agencies involved are unbalanced. We are skeptical about the capacity of a small expert group to prepare a sound and comprehensive four-year regional development program in a short span of two weeks. But we recognize the Government's earnestness in doing something quickly for the rural poor and we think this program can be improved in several directions. It is here that we see an initial role for the Bank.

13. In many regions the potential for developing agricultural production is good, but serious limitation exists on the per farm income due to the limited size of farm unit, quite commonly not exceeding 2 hectares in rainfed areas. Undoubtedly this is the most difficult aspect of the rural program but useful experience and positive results have been obtained in the Puebla project, initially sponsored by the Rockefeller Foundation. The project demonstrated that with improved seed, fertilizer and extension yields and consequently income could be substantially increased in a relatively harsh environment. These elements have received inadequate attention in the present program. One reason is probably because the responsible technical ministry, the Agriculture Ministry, is weak and poorly staffed.



14. In our view, the main weaknesses of the present integrated program lie in:

- i. inadequate administrative and institutional arrangements at the local, regional, state and federal levels;
- ii. inadequate (rather, hardly any) participation of the people in evolution and implementation of the program;
- iii. Lack of linkage of the infrastructure investments with directly productive investments including extension services, credit, production inputs, marketing arrangements; and
- iv. the lack of a training program and manpower planning for undertaking a program of the magnitude the Government has in mind.

15. However, we believe that these shortcomings can be remedied and accordingly we recommend that a group of Bank staff work closely with the Government in evolving better regional programs within the present structure of the overall program. This should first be tested in a limited region before moving ahead on a large scale. Fortunately, for several months now, we have been working with the Bank of Mexico in developing an agricultural credit project in which a sub-project is directed at the small farmers and the ejidatarios of specified regions, including many of Mexico's poorest areas. The project is scheduled to be presented to the Board in May 1973 and would cover about one-half of Mexico. Under this credit project, arrangements for credit, extension services and production inputs will be developed. It is our recommendation that two or three Bank staff members work with the Government in developing integrated development programs in areas also covered by the credit sub-project. The Government has reacted favorably to the initial soundings and both the Presidencia - Hacienda and the Minister for Public Works have expressed their interest in working with the Bank. The former have already followed up by telephone, offering to write a formal request for such assistance. Our role should be in helping the Government develop a sound program and we suggest that we leave it to the Government to resolve the conflict among the rival claimants, but it should be noted that these rivalries are fierce and that it remains to be seen when and how they will be resolved. <sup>1/</sup>

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<sup>1/</sup> Thus, as soon as we communicated to the Minister of Public Works what our recommendation to the Bank would be, he suggested that SOP would submit integrated regional programs to the Bank for financing, whether in addition to, or instead of, those of the Presidencia - Hacienda program, was not stated. Thus, it is possible that the Bank will be under pressure from SOP to finance for them the kind of programs presently done by Presidencia - Hacienda. The latter would object to this. We have taken the line that it is the character and quality of the program that the Bank will address itself to, and that the Government must sort out jurisdictional issues.

Recommendations

16. In our view the Bank can play a positive role in the rural development program of Mexico. Presence of the Bank might help ensure adoption of a balanced development program and the production aspect at the farm level would be kept in focus. Bank role can be particularly important in the conceptual approach and institution building. We recommend that two or three staff members be assigned to work with the Government for a period of 2-3 months to evolve an experimental program covering 10-15 "regions" of integrated development in Mexico in areas where credit and extension services would be assured with a view to having a phased program, with subsequent lending contingent on the experience of the experiment. The Bank could then appraise a project - consisting possibly of 10-15 regions - for a possible loan. The appraisal justification criteria would require some further thought.

cc: Messrs. Alter  
Baum  
Gutiérrez  
Knox  
Evans  
van der Tak

DDutt:mgf

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16

## OFFICE MEMORANDUM

TO: Memorandum for the Record

DATE: October 2, 1973

FROM: John A. Holsen, Senior Economist, LAC I (drafted in Nairobi)

SUBJECT: Meeting of Mr. McNamara with the Mexican Delegation in Nairobi  
on September 26, 1973

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1. Mr. McNamara met with José López Portillo, recently appointed Minister of Finance and Public Credit, on September 26, 1973. He was accompanied by Miguel de la Madrid, the Director General for Credit, and by Rafael Izquierdo, Advisor to the Minister. Also present were Messrs. Knapp, Alter and Holsen.
2. Minister López Portillo, opening the discussion, noted that the thoughts in Mr. McNamara's speech to the Annual Meeting reflected a reality close to Mexico and in accord with its experience. The problem of inflation was of particular concern at the moment and the Government had adopted a sixteen-point program to bring it under control. The Government was determined that this process would not adversely affect the poorer classes; consequently increases were being authorized in wages in both the public and private sector and also in the prices of corn and beans which are widely produced by small farmers.
3. Regarding the situation of small farmers in Mexico, the Minister explained that the system of ejidos, a system of land tenure established in Article 27 of the Constitution, had resulted in a continuing fragmentation of land holdings which prevented the use of modern farm inputs and techniques. The solution the Government was adopting was a system of "ejido enterprises". In these enterprises, each individual contributed the land which he had the right to use; this entitled him to half the product from that land. He received the other half as well if he also contributed his labor to the enterprise. This system was developing slowly but with success. It was an experiment in collective enterprise in which individual rights were maintained, but work was done in common. The Minister said that the present food crisis demanded that land be cultivated efficiently; in the future the world would insist upon a law against idle land since this was a crime against humanity. He invited the Bank to send a mission to study the system of "ejido enterprises".
4. Mr. McNamara noted that the Bank would be happy to send a mission if the Government wished. He asked Mr. Alter to provide him a note by October 15 on how to approach the subject; he suggested that Wolf Ladejinsky or Sir John Crawford might be asked to participate.
5. Minister López Portillo stressed the importance of increasing agricultural production. Mr. McNamara said that in Iran the Bank was studying the appropriate organizational form to maximize production, but that it did not yet have the solution.

6. The Minister then thanked the Bank for its help in other sectors, mentioning the recent steel project in particular. He also noted that his Government had resolved the problem of electric power rates; when he got back to Mexico, if not before, adjustments would be made to attain the level and the structure discussed with the Bank. He said that, upon entering his present position, he decided it was necessary to study the question of fiscal reform and, while this was being done, to increase public sector income by tariff and price policies.

7. Mr. McNamara indicated he was glad to hear of the steps being taken as he could see a long-run need for greater revenues. The Minister replied that this was his fundamental problem and that he was in full agreement. He noted that the increase in electricity rates fulfilled a commitment he had earlier made as Director General of the Federal Electricity Commission. He could not yet speak definitely about petroleum product prices. The question was a difficult one since the Government was worried about the psychological effects following the price "explosion" in the middle of the year; consequently the decision had been postponed.

8. Mr. McNamara said that the two topics discussed by the Minister were the ones most important for the Bank. These were (a) increasing production in rural areas and, by that means, assuring a better income distribution and (b) implementing rate, tax and expenditure control policies which would assure a sound and reliable source of funds for investments. Minister López Portillo concluded the meeting by saying that these were the main elements of his program.

cc: Mr. Alter, Regional Vice President, LAC  
Mr. Knox, Projects Director, LAC P  
Mr. Lerdaun, Acting Director, LAC I  
Mr. Christoffersen, Division Chief, Rural Dev. Division,  
Agriculture and Rural Dev. Department  
Division Chiefs of LAC Projects Department  
Mexico Division

JAHolsen:pa/mgf

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September 28, 1974

Note for the File

Mr. McNamara met with Mr. Ernesto Fernandez Hurtado, Director General, Bank of Mexico, and Mr. Alfredo Phillips Olmedo, Manager, Bank of Mexico, on Saturday, September 28. Mr. Ernest Stern was present from the Bank.

The topic of discussion was the work program for the proposed Development Council. (*Committee?*)

There will be no formal memorandum of conversation of the meeting (per Mr. Stern).

*B.M.M.*

B. M. Moore

18.



DECLASSIFIED  
OFFICE MEMORANDUM  
MAY 8 7 2018CONFIDENTIAL

TO: Memorandum for the Record WBG ARCHIVES DATE: September 3, 1975

FROM: Shiv S. Kapur, Division Chief, LAC I

SUBJECT: Meeting of Mr. McNamara with the Mexican Delegation on September 2, 1975

1. Mr. McNamara met with Mr. Mario Ramon Beteta, Deputy Minister of Finance, on September 2, 1975. Mr. Beteta was accompanied by Messrs. Ernesto Fernandez Hurtado, Director General of the Bank of Mexico, and Gustavo Romero Kolbeck, Director General of Nafinsa. Also present were Messrs. Knapp, Krieger, Lerdaun and Kapur.

2. Mr. McNamara opened the meeting by referring to our recent economic mission to Mexico and its disquieting conclusions in respect of economic trends and developments as a whole. He asked Mr. Beteta for his reading of the situation. Mr. Beteta accepted that certain indices of economic performance give cause for disquiet: the President of Mexico in his State of the Union message only the previous day recognized the heavy fiscal and balance of payments deficits and the inflation which the country had been suffering. As Mr. Beteta put it, Mexico had caught the international infection of inflation, although he did not disown responsibility of domestic economic policies for contributing to it.

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3. Mr. Beteta, however, quoted Mr. McNamara to say that, for the developing countries, alternatives are not abundant and such countries consequently face an extremely difficult situation. So far as Mexico is concerned, Mr. Beteta claimed that he was not sure if the country was not achieving its objectives. In this connection he pointed to the developments in the fields of petroleum, transportation and the production of food, all of which he thought would change the prospects for the future. The fiscal and balance of payments deficits were undoubtedly larger than anticipated; Mexico could not however relinquish medium and long-term objectives in the face of present difficulties. The country could at least claim to have maintained a positive rate of growth, unlike so many other countries all over the world, and he hoped this growth will continue. While Mexico would look to continued external help, Mr. Beteta hoped that the need for such help would diminish as the United States' economy picked up momentum and Mexico's exports grew in volume. In the meantime, the Government planned to impose more stringent budgetary discipline and to reduce current expenditures.

4. Despite the above presentation, Mr. McNamara thought that the situation in respect of public expenditures, balance of payments and external debt management, which was already unsatisfactory, could easily become acute. If, further, the OECD countries do not grow as anticipated then, he wondered, what the Mexican strategy would be. Mr. Beteta responded that the Government will then have to take stock of the situation and resort to necessary measures. He alluded to an exchange rate change

by quoting the Mexican President to say that the present rate will be maintained; the Government plans, instead, to achieve similar objectives by reducing imports and increasing exports. The exchange rate question was a very sensitive political and social issue in the country, especially at the present time when in another about six weeks the next presidential candidate would be revealed. This, Mr. Beteta stated, was "certainly not the time for such decisions." However, he added that the Government was aware of the problems, was discussing them and was trying to find satisfactory solutions. It will adopt what measures are found necessary.

5. In the meantime, adverting to Mexico's heavy borrowing, he claimed that Mexico remained a good credit risk and that there was no option to increased indebtedness. Whether borrowing on this scale would be necessary in the future he could not tell. In respect of domestic policies, he again reiterated the Government's intention to impose strict discipline through the budget for 1976 which will also institute other measures as may be necessary. The Committee for Public Expenditure, similar to that for Investment and Financing, will be used intensively to curb the growth of current expenditures; while this Committee has been in existence for some time, it has not been used in the past as an effective mechanism to monitor public expenditures.

6. Mr. McNamara commented that he understood the political problems of development. However, the Bank has a large lending program in Mexico; and we have to continually borrow in the world markets to sustain our operations. We have therefore to be extremely careful in our lending and would have to adjust our lending to Mexico to the country's economic performance. He recognized the medium and long-term strength of the Mexican economy; there is however no doubt that a serious short-term problem exists. The Bank's lending for the time being may be therefore less than it might otherwise be and judgments will be made in response to the policies and actions taken by the Government to improve the situation. Mr. McNamara however added that he hoped this situation will not last long. He held forth a firm assurance to Mr. Beteta that the Bank has no wish to compound the Mexican problems in any manner; what he foresaw was a situation of action and inter-action between the Government's economic management and levels of Bank lending. Mr. Krieger, he said, will remain in close contact with the Government as its 1976 economic program is formulated. In this connection, he expressed particular concern about Mexican exports and the need to maintain their competitiveness.

7. As to Mexico's exports prospects, Mr. Beteta claimed that their position was not deteriorating in relation to others. A lot, of course, depends on how other economies behave. Mr. Beteta expressed his satisfaction

at the Bank's lending posture outlined above. He said that he was happy to hear the Bank will, in its lending, follow Mexican developments. In addition to capital transfers, Mexico had received wise counsel from the Bank in the past which he thought had been most beneficial. He hoped such expert advice would also be forthcoming in the future. On its part, Mexico will continue to offer its full cooperation in the Bank's investigative and other work in the country.

8. Mr. McNamara expressed his appreciation of the openness of the Bank's relations with Mexico; in addition to our exchanges on economic management, this is fully reflected in our very large lending program to that country. Mexico however faced very difficult 6 - 12 months ahead and could encounter serious debt management problems. He urged Mr. Beteta that the Government watch for this most carefully.

9. In closing, Mr. Beteta accepted that what Mr. McNamara had stated was the objective truth. On the other side of the picture, however, were excellent petroleum prospects and substantial improvements which had already been brought about in agricultural production. For the future, Mexico plans to assure that (i) the forthcoming budget would be in accord with the country's economic circumstances; (ii) the budget would reflect severe fiscal discipline and a reduction in the growth rate of current expenditures; and (iii) priority will be given to completing productive investment projects.

cc: Mr. McNamara's Office  
Messrs. Knapp  
Krieger  
Lerdau  
Knox  
Blaxall  
Glaessner  
Malone  
Mexico Division

SSKapur: rmd

Biographical Sketches of Senior Delegation Members

Secretaria de Hacienda y Credito Publico:

Beteta, Mario Ramon 1/

Deputy Minister of Finance.

Studied law in the Mexican Autonomous University and economics in the Wisconsin University.

During the 1950s he started his career in the Banco de Mexico as an economist, reaching the level of Deputy Director in 1965.

In the late 1960s he joined the Ministry of Finance as Director General of Credit, and since 1970 he holds his present position.

Up to the late 1960s he has participated in numerous courses on economics and law in the Mexican Autonomous University and the Latin American Center of Monetary Studies (CEMLA).

de la Madrid, Miguel

Director General of Public Credit.

He has economics degrees from U.S. universities.

Before his present appointment he was Finance

Director of the state-owned petroleum company, PEMEX (1971-72).

During the previous administration he was Deputy Director of Public Credit in the Ministry of Finance.

His professional career started in the Bank of Mexico.

Izquierdo, Rafael

Advisor to the Bank of Mexico and Ministry of Finance.

Director General of the Bank of Mexico.

He is one of the most prominent Mexican economists and has done an important work on protection in Mexico.

Bank of Mexico:

Fernández Hurtado, Ernesto:

Director General of Bank of Mexico since 1970. Economist, banker, degree Mexican Autonomous University and Yale.

With Bank of Mexico over 25 years.

Numerous posts.

Professor of Economics Mexican Autonomous University.

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1/ Not yet confirmed.

Phillips, Alfredo

Manager for International Relations in the Bank of Mexico.  
He was the Mexican Executive Director at the International Monetary Fund (1968-70) and has economics degrees from U.S. universities.

Nacional Financiera, S. A.:

✓ Romero Kolbeck, Gustavo

Director General of Nacional Financiera, S. A. Studied economics at George Washington University and the Mexican Autonomous University, where he still teaches.

His career has been mainly in academia. He founded in 1954 the Mexican Academy of Human Sciences, and has lectured in various Mexican and U.S. universities.

Director General of several business publications, including "Business Trends" and "Expansion" (1960-70).

Former Ambassador to Japan (1971-73).

Galicia Estrada, Pedro

Manager, International Projects Department, Nacional Financiera, S. A.  
Studied communications and Economics at the Mexican Autonomous University and Stanford University.  
He has made a career in Nacional Financiera since 1960, and has since represented that institution and his government in various international negotiations.

Attachments

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## OFFICE MEMORANDUM

TO: Memorandum for the Record

DATE: October 13, 1976

FROM: John Holsen *JH*

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MAY 07 2013

SUBJECT: MEXICO : Annual Meetings

WBG ARCHIVES

1. Mr. McNamara met with the Mexican Delegation to the Annual Meetings in Manila on Tuesday, October 5. The spokesman for the Mexican Delegation was Mr. Ernesto Fernandez Hurtado, Director General of the Banco de Mexico. He was accompanied by Messrs. Gustavo Romero Kolbeck, Alfredo Phillips, Pedro Galicia and Eduardo Pesqueira. Messrs. Knapp, Krieger, Lerchau, Burmester and Holsen also attended for the Bank.
2. Sr. Hurtado opened the discussion by expressing the regrets of the Minister of Finance for his inability to come to the meeting; he was, however, in the middle of the new economic program and it was impossible for him to attend. Mr. McNamara expressed his understanding and congratulated the Mexican authorities on the actions they had taken. Sr. Hurtado said that the shock of the devaluation was being absorbed and that the incoming President's actions would be consistent with the present program; he stressed the importance of not only the present measures but what had to be done during the next three years.
3. Mr. McNamara asked Sr. Hurtado about the recent wage settlement. The latter replied that, while he didn't like it, the settlement was politically the best obtainable; the adjustment was large, but future wage policy would be what really counted. Mr. McNamara noted that the devaluation would be wasted unless followed by proper domestic policies. He asked about the public sector deficit and was told the most that could be done this year would be to moderate the trend. The President had, however, authorized a strict program regarding current expenditures. Sr. Hurtado said the government had made a major effort to raise revenues, but no savings resulted because of the growth of current expenditures, public sector investment was being financed entirely by borrowing. The incoming President, however, recognized the importance of increasing public sector savings.
4. Mr. McNamara asked about the prospects for Mexico's obtaining the borrowing it needed from private sources. Sr. Hurtado said the bankers were observing how the situation developed; Mexico had to prove its will to control the current account of the balance of payments. Mr. McNamara noted the warnings by several speakers during the meetings and said the private bankers would be carefully watching their loans to the LDC's. Sr. Hurtado reported that the bankers had reacted favorably to the recent steps and to the agreement with the IMF. Mr. McNamara concluded this part of the discussion by saying the Bank would be happy to work with the Mexican authorities, but they needed to make decisions regarding their development program.
5. Mr. McNamara then turned the conversation to the serious problems in financing the Bank. Mexico and the other Latin American nations should help the OECD countries realize the importance of this problem. It was important to make their views known to the U.S. Government. The North-South dialogue provided opportunities; all possibilities should be used.

October 13, 1976

6. Sr. Hurtado asked why the U.S. was so reluctant to increase the Bank's resources. Mr. McNamara explained this in terms of a short-run problem in Congress (while the administration was holding back on domestic programs) and a longer-run general disaffection with foreign aid and doubts about its effectiveness.

7. Mr. Hurtado noted that commercial bank financing for the developing countries would be better linked to development finance from the Bank than to Stand-By Arrangements with the IMF; the Bank's country studies would help. Mr. McNamara agreed that one of the Bank's functions was to facilitate soundly based private flows; if related to prudently managed economics, the large increase in private financing presented in Mr. McNamara's speech would be justified. Sr. Hurtado noted that the Bank's sector studies were helpful. Mr. McNamara said that the Bank's economic reports might be made available to private banks; Sr. Hurtado noted that some of the details in the reports might not be appropriate for such distribution.

8. Concluding the discussion of the Bank's financing problem, Mr. McNamara discussed the tactics which might be used. He said that he was, philosophically speaking, in full agreement with the LDC desire for a larger proportion of votes in the Bank. In practice, however, votes were not so important since the most difficult questions related to money and in these cases success didn't depend upon LDC voting power. The discussion over votes could delay the general capital increase (as it did the agreement on the selective increase); it was important, also, to find a way to raise the \$5.8 billion ceiling for the next fiscal year. Mr. McNamara would support the Latin Americans in maintaining three directors on the Board, even if this meant a larger Board, but he hoped the issue of votes would not be pressed to the point that it delayed the needed expansion in the Bank's lending capacity.

cc: Mr. Burmester (Mr. McNamara's office)  
Mr. Knapp  
Mr. Krieger  
Mr. Lerdau  
Mr. van der Meer  
Mr. Dutt

JHolsen:jd



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## OFFICE MEMORANDUM

TO: Memorandum for the Record

DATE: February 11, 1977

FROM: Devbrat Dutt, <sup>7/2/77</sup> ~~Division~~ Chief, LACIASUBJECT: MEXICO: Summary Record of Discussions between Mr. Moctezuma, the Finance Minister, and Mr. McNamara - February 9, 1977

1. Mr. Julio Rodolfo Moctezuma Cid, the Finance Minister, called on Mr. McNamara on Wednesday, February 9, 1977. The Minister was accompanied by Messrs. Romero Kolbeck, Director General of the Bank of Mexico; Leopoldo Solis and Alfredo Phillips-Olmedo also from the Bank of Mexico; Miguel de la Madrid, Deputy Minister of Finance; and Mr. Pesqueira, the Executive Director for Mexico. Messrs. Knapp, van der Meer and Dutt were present.

2. Mr. Moctezuma expressed his appreciation at their intimate relations with the Bank which he wanted to be further strengthened. Then he, along with Messrs. Romero Kolbeck and Miguel de la Madrid, explained that a large scale reorganization of the administration was currently taking place in Mexico, and the expenditure policies of the Government were being reviewed. This was a period of revision of priorities and for reflection, and the Treasury along with the Ministry of Programming and Budgeting and executing agencies were in the process of reviewing several projects for a proper definition of the Government's position at the highest level. They proposed to redefine Las Truchas II and proceed with a modified steel project, hopefully with continued access to the Bank loan. The Rio Bravo Irrigation project has made some progress and the water rate issue has been resolved, but the scope of the project is proposed to be changed. The Highway project was also under review and the Mexicans expected to present to the Bank precise proposals on the on-going projects in about a month.

3. Mr. McNamara stated that he did not wish to give the impression that the Bank was pressing the Government to proceed with these three projects, or, for that matter, any other Bank supported project; the projects they finally decide to implement should be clearly their projects and of their interest. However, he would be interested in knowing the Mexican thinking to be able to plan the Bank's own work.

4. The discussions then turned to the five projects for which the Mexican authorities had sought Bank assistance and which have already been appraised (these are Ports II, Family Planning, Urban Development, Rural Development and Baja California Tourism). Mr. McNamara enquired from Mr. Moctezuma what the Government plans were for the processing of these projects.

5. Mr. Moctezuma explained the composition of the Economic Cabinet and stated that the Government's priorities were clearly the development of energy and agriculture sectors, and that each of the five projects under consideration by the Bank would be examined in detail. For some (he specifically mentioned the Ports project) no agreement has yet been reached and the issues were still being examined. Working groups will analyze each project and submit proposals for decision of the Economic Cabinet. He expected that the Bank would be informed of the Government's position on this package in one month to six weeks.

6. Mr. McNamara stated that it was fair that the Government should examine and propose projects clearly of its interest. However, with a slippage of one and a half months the projects will not be ready for final action in FY77. He encouraged the Government to reflect on each and take the proper decision; the final program should be the Government's program. The Bank was ready to resume action on the processing of any of these projects as soon as a decision to proceed had been made by the Government.

#### Economy

7. At this stage Mr. McNamara asked Mr. Moctezuma about the outlook for the economy, especially the success in tackling the serious and complex problems it had inherited.

8. Mr. Moctezuma explained at some length the post-September (1976) developments, the crisis of confidence and the resulting loss of financial savings. While the situation was complex, he was optimistic on the prospects for the economy in the Lopez Portillo administration; the general outlook was good and the confidence in the economy was being restored; the liabilities of the banking system were increasing.

9. Mr. McNamara observed that in the recent years there has been concern on the tax revenues, pricing of public enterprise goods and services, and on expenditure control. Mr. Moctezuma explained that the 1977 budget (the adjusted rather than the original) was not an expansionary budget. In nominal terms the expenditure budget was 30 percent higher than in 1976, but in real terms there was no increase. He stated that after one made adjustments for three factors--higher foreign debt service payments; the full annual impact of salary increases granted in September 1976, particularly to CFE and PEMEX staff; and the higher Peso costs of machinery to be imported by PEMEX for the petroleum sector--the 1977 budget was rather restrictive. The Congress has been approached for authorization on four fiscal measures: (i) tax exemption for low wage earners (those with income up to two times the statutory minimum salary), (ii) tax credit for investment in priority sectors, equivalent to 10 percent of value of machinery, (iii) 50 percent tax on excess profits, and (iv) new taxes on luxury and non-essential goods.

10. Mr. Moctezuma went on to say that a new committee on "prices and tariffs of public sector enterprises" has been set up, and the Government hoped to raise additional 20 billion Mex\$ resources during the year, of which measures to yield Mex\$8 - 9 billion have already been taken. Some of the public sector problems are being cleared up. The September (1976) salary increase of 23 percent was on top of the other increases and amounted to as much as 40 percent for some enterprises. An evidence of the marked improvement of Government's bargaining capacity was the minimum wage adjustment this year, restricted to 10 percent. This was not a net increase when changes in prices of some basic goods are taken into account. The whole relationship between labor and Government was undergoing a change for the better. The Government has also reached agreement on a 'program of basic products' which would protect the labor in purchasing essential goods. Mr. Moctezuma then stated that there has been a marked change in the inflation rate as well; in October and November the price index increased at a monthly rate of 8 percent, but despite the normally high liquidity in December, the inflation rate was 3%, and declined further to 2% in January.

11. Concluding his presentation, Mr. Moctezuma stated that the Lopez Portillo Administration was presently preparing a comprehensive program for the economy. An agricultural production program has just been started, with specific objectives and responsibilities for the Federal and State Governments. A similar program for education has been agreed upon. Ten convenios for industrial production in the private sector have been signed, and consensus has been reached with the three most important political groups in the country--the labor, the peasants and the political party--in support of a comprehensive family planning program.

12. Mr. McNamara thanked Mr. Moctezuma for this presentation, adding that it was an impressive record for the short period of the new administration. He said that domestic resource mobilization was very important; historically Mexico has a record of rather low levels of public revenues, and Mexico needed those along with earnings of public enterprises badly. Mr. McNamara said he looked forward to his meeting with Mr. Lopez Portillo next week.

cleared with and cc: Mr. van der Meer

cc: Messrs. McNamara  
Knapp  
Krieger (o/r)  
Lerdau (o/r)  
Holsen/Nowicki

DDutt:crm

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Adalbert Krieger

MEXICO: Meetings with the Mexican Delegation on February 17, 1977

1. Following the meeting between the President of Mexico, Lic. Lopez Portillo, and Mr. McNamara on Thursday, February 17, I met with a Mexican delegation consisting of Messrs. Miguel de la Madrid, Under-Secretary of Finance, Alfredo Phillips of the Bank of Mexico, Antonio Enriquez Savignac, Under-Secretary of Tourism and Pesqueira, Executive Director; Messrs. Wyss, Goffin, Renger, Nowicki, Kendall, Villarzu and Dutt from the Bank were present.
2. I raised again the same topics that Mr. McNamara had discussed with President Lopez Portillo earlier in the morning and asked Mr. de la Madrid if he could give us his comments on the status of the three loans (SICARTSA II, Rio Bravo Irrigation and the Highways project), as well as the Government's decision on the loans proposed for five new projects (Ports II, Maternal-Child Health Care and Family Planning, Urban Development, Rural Development and Baja California Tourism).
3. Mr. de la Madrid indicated that with the exception of the Baja California Tourism project, which the Government was ratifying, and a new tourism development loan to FONATUR (a trust fund for tourism development), the other projects were under review of the Government. He said that as stated by Mr. Moctezuma, Minister of Finance, during his recent visit to Mr. McNamara, the authorities needed approximately four to six weeks to reach a decision, and he requested us to grant them the necessary time. Even though my colleagues and I tried to open a discussion on these projects, Mr. de la Madrid maintained a firm position and indicated that they were not in a position to discuss these projects in detail until a decision had been reached by the Government.
4. Mr. de la Madrid and his colleagues then referred to the serious balance of payments problem of Mexico, the importance the Government attaches to expansion of the tourism sector as a means of quickly increasing foreign exchange earning and requested a line of credit for FONATUR to finance its credit operations for promoting investment in hotels and other superstructure facilities for foreign tourists. (Please see my memorandum to Mr. Knapp dated February 17, explaining the proposal).

Meeting with Mr. Knapp

5. Later the Mexican delegation went to see Mr. Knapp; Mr. Dutt and the writer were also present. After informing him that they were ready to negotiate the Baja California tourism infrastructure project, the

Mexicans stated that during the morning meeting between President Lopez Portillo and McNamara, the Secretary of Tourism (Mr. Rossell de la Lama) had sought from the Bank a line of credit to finance hotel and other superstructure investments. Mr. de la Madrid explained that Mexico lacked hotel facilities fully to take advantage of their tourism potential, and were facing serious shortages of both foreign and domestic resources to finance the tourism sector adequately. Mr. Enriquez Savignac added that private banking funds were difficult to raise by the industry and the Government had to intervene by providing rediscounting facilities through the FONATUR to help the industry. In a period of 3 years 22,000 hotel rooms had been built under the program, but a much larger construction program was necessary to cater to the rising demand. The Mexicans added that the loan they were now seeking was not very different from similar lines of credit that the Bank was providing for development of agriculture (through the FONDO), or of industry (through FONEI), and that the proposed project will be most useful in enabling Mexico tackle their balance of payments and employment problems.

6. Mr. Knapp responded by saying that he was not doubting the attractiveness of the project, and that the Bank has done some similar operations in other countries, but both Mr. McNamara and he were concerned that instead of looking at the overall range of possibilities of borrowing from the Bank, and deciding a package best answering the needs of Mexico, a single project was being proposed. Within the overall borrowing program from the Bank, Mexico should weigh the inter se priorities, and he was not sure that the proposed operation would be of the highest priority. Mr. Knapp then offered some suggestions where the Mexican priorities might lie: Agricultural development, food production and improving the income in rural areas was obviously of the highest priority; then came water management for agriculture and potable, the poor both in the urban and rural areas needed safe drinking water facilities; basic infrastructure development - energy, transportation, and regional development to stem the inflow of migrants into the Mexico City metropolitan area - were important; family planning was another obvious priority. The scarce Bank resources should be used in support of these priority investments, for which other external sources would not be readily available, and only after that should come direct financing of industrial and tourism projects. Overall priority, rather than an individual project, should be looked at in deciding the Bank - Mexico relationship, and he advised the Mexicans to work out a strategy for medium and long-term development with collaboration of the Bank.

7. The Mexican delegation accepted the importance of planning and stated that integrated development programs were being prepared but it

will take several months before a comprehensive program that could stand scrutiny would be ready. Mr. de la Madrid reiterated that the Government wanted to have a few more weeks until they could communicate to us its decision about the on-going lending program, as well as its views regarding the sectors that contribute to the Mexican financial and investment development. In the meantime, Mexico faced a very difficult economic situation, rather was passing through a crisis, and needed flexibility and understanding from the Bank in solving its immediate problems. They reiterated their request for a tourism development loan, and stated that (a) such a project would be ready for appraisal within 2 months, (b) 90-95% of the hotels to be assisted are estimated to be in the private sector, (c) about 15 years would be required by the investors to repay the credits, (d) the project will have a high employment impact, with wide geographic dispersion of benefits.

8. Mr. de la Madrid referred again to the tourism sector and requested Mr. Knapp's support for a credit project to FONATUR to finance the construction of new hotels. Mr. Knapp replied that he would give special consideration to this request but reiterated the need to obtain from the Mexican Government a decision on the important subjects of the lending program mentioned above. He also observed that the proposed project should be attractive for co-financing with other banks.

Attachment: Memorandum dated February 17, 1977 from Mr. Krieger to Mr. Knapp


cc: Messrs. McNamara  
Knapp  
Tolbert  
Lerdau  
van der Meer  
Holsen  
Dutt  
Perez

AKrieger/DDutt:sr



Mr. J. Burke Knapp

February 17, 1977

Adalbert Krieger 

MEXICO: Possible Tourism Development Loan

1. This morning the Minister of Tourism asked Mr. McNamara to consider a Bank loan to FONATUR (a trust fund for tourism development) to finance its credit operations. This would be in addition to a loan to FONATUR for tourism infrastructure development which was appraised in October. In concurrence with the Tourism Projects Department, we are now proposing to further explore the possibility of such a tourism development loan of US\$30-50 million. The purpose of this memorandum is to seek your approval for initiating serious conversations with the Government along the lines summarized below leading to an early appraisal of the project.

Tourism Sector Potential

2. Foreign visitor arrivals increased annually at an average rate of 10.4 percent in the last 15 years and totalled 3.2 million in 1975. Earnings from tourism amounted to US\$800 million and is now Mexico's largest source of foreign exchange earnings (13% of exports of goods and non-factor services). The annual rate of growth of foreign arrivals is expected to resume at a rate of 6 to 10 percent over the next several years. Therefore, provided the necessary investments can be timely funded and carried out, and the right policies are followed, the prospects of the tourist industry are bright.

Sector Resource Requirements

3. As the demand for tourism services increases, new hotels will have to be constructed and numerous other facilities and services will have to be expanded. For the present, estimates of capital requirements are available only for the hotel industry but these already show a substantial financial gap, as broadly identified below.

4. Utilization of available accommodations (175,000 rooms in early 1976, of which 76,000 are considered suitable for international visitors) is already high in major destination areas. Assuming, however, that some of the increase in visitors to Mexico can be absorbed by a higher utilization of hotel capacity and that the rate of annual increase in visitor arrivals is only 6 percent, the recent Bank tourism mission has calculated that a total of 18,000 additional international-class hotel rooms would still be required between 1977 and 1980. This would involve a total investment of US\$410 million.

5. Normally, the capital structure of new hotels is 35 percent equity and 65 percent loans. With the exception of a few large hotels, most of the equity is put up by Mexicans; foreign equity represented less than 10 percent of total equity capital in the hotel industry since 1973. Loan capital is practically all Mexican. There are only a few cases of foreign loans for hotel development (which representing only about 5 percent of total hotel loan capital since 1973). About 80 percent of loan capital for hotel construction has been financed by FONATUR since 1973 (about US\$230 million to finance 19,000 rooms).

6. FONATUR discounts term loans at 90% and the remaining 10% is financed by its financial intermediaries. The interest spread for the financial intermediaries is currently in the range of 2-3%, depending on the terms and amounts of the loans. The ultimate borrowers receive the discounted term loans at an interest rate of 10.0 - 12.5% for 10-15 years, including a grace period of 2-3 years.

7. The source of funds for FONATUR's credit operations has been the Federal budget, Banco de Mexico bond issues and retained earnings from its credit operations. As of August 31, 1976, FONATUR's resources amounted to Mex\$2.9 billion (US\$232.0 million), including Mex\$1.1 billion (US\$88.0 million) funded by the Government as equity contribution, Mex\$1.7 billion (US\$136 million) raised by Banco de Mexico through bond issues at an interest rate of 8% for a term of 8 years, and Mex\$0.1 billion (US\$8.0 million) earned from its operations.

8. Although hotel financing from foreign borrowings might increase in the future, given the brighter prospects of tourism in Mexico, the mission established through contacts with foreign banks in Mexico that such increase would not be sizeable over the next several years. On the other hand, private savings are not expected to be large enough to meet the requirements of the private and public investors in Mexico for several years to come. It appears that the industry will have to continue to rely substantially on term loans from FONATUR: it is estimated that FONATUR will have to provide 58 percent of total 1977-1980 capital requirements (or about US\$240 million). Thus a Bank loan would not substitute private capital for the industry.

#### A Tourism Development Loan

9. Our present tourism operations are centered on Government financed major infrastructure development in new tourism poles, with a period of several years required to achieve full potential. In the circumstances, it seems worthwhile to consider a loan to channel into the sector funds not otherwise available to private investors or public institutions for the purpose of expanding the capacity of hotels and other tourism facilities and services, including minor infrastructure, transportation, recreation, shops and restaurants at existing sites and handicraft production. FONATUR would be a well qualified intermediary for this loan. As of August 31, 1976,

FONATUR had approved 378 ~~percent~~ applications for a total amount of Mex\$2.8 billion (US\$224 million equivalent at an exchange rate of US\$1 = Mex\$12.50) to finance approximately 19,000 rooms throughout the country, most of it in the last four years. Of this total, Mex\$1,9 billion (US\$152 million equivalent) had been disbursed by September 1976. Applications for credit in the amount of Mex\$500.0 million were pending (US\$40.0 million).

10. The proposed loan would be used to finance the foreign exchange component of FONATUR lending operations. The individual subprojects would have to show acceptable economic rates of return, in addition to meeting sound technical and financial criteria. FONATUR's on-lending interest rate structure to final borrowers would be closely linked with the cost of alternative funds to encourage efficient resource allocation, strengthen FONATUR's financial performance and increase its capacity to mobilize resources.

11. The proposed project would rapidly help to strengthen Mexico's balance of payments by supporting attractive subprojects that might otherwise not be undertaken due to scarcity of adequate long-term financing. Additionally, this operation would be instrumental in exploring ways to mobilize additional financing resources from commercial banks, and onlending arrangements that would encourage entry in the sector by investors now shut out by prohibitively high equity requirements. Because Mexico's tourism assets are widely dispersed, their development will also help in reaching a more balanced regional distribution of economic activity. Furthermore, most of the additional employment generated will be drawn from the unskilled sector of the population after a relatively short training requiring little investment by the industry or the Government; tourism projects in Mexico easily meet the urban poverty test of the recently issued capital labbr ratio guidelines.

12. On institution building grounds, the proposed project would be instrumental in improving the appraisal criteria, techniques and follow-up procedures of FONATUR thus contributing to improved design and better capacity utilization of projects. Tourism data gathering and analysis would be undertaken more systematically by FONATUR so as to promote tourism investments best suited to foreign visitors.

13. Loans with similar purposes have been made for Ivory Coast (\$9.7 million in FY75) and Morocco (\$25 million in FY76).

cleared with and cc: Mr. Tolbert

cc: Mr. Lerdau (o/r)

 MvanGent:crm

## OFFICE MEMORANDUM

TO: Memorandum for the Record

FROM: Adalbert Krieger *AK*

SUBJECT: MEXICO: Meeting at Blair House Between the President of Mexico  
Lic. Lopez Portillo and Mr. McNamara

DATE: February 23, 1977

A meeting was held between 8:30 and 9:30 on February 17, 1977. A list of Mexican officials attending is included in the attached annex. Mr. McNamara was accompanied by myself.

The President of Mexico opened the meeting by thanking the Bank for the support it has given to Mexico in the past and for the understanding it has shown while his country faced difficult circumstances. Mr. Lopez Portillo then explained his views, which he had expressed on several occasions during his visit, on the problems which Mexico faces. He said that Mexico must attempt to resolve problems which are inter-related; it must expand exports at the same time that it takes steps to improve the efficiency of production. This in turn is related to another important problem: unemployment. Mr. Lopez Portillo referred to his conversations with President Carter and other U.S. authorities regarding the issue of illegal immigration to the U.S. This problem could only be resolved, he said, if employment opportunities in Mexico are improved, and for this the understanding and cooperation of the U.S. is required.

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In his reply, Mr. McNamara first congratulated President Lopez Portillo for the courageous steps taken by his administration during its first few weeks in office to resolve the short-term problems faced by Mexico. It is clear, he said, that the new administration had shown its determination to face the financial crisis which has affected Mexico by taking monetary and fiscal measures and obtaining the IMF's support through an Extended Fund Facility for 1977-79. Mr. McNamara then referred to longer-term economic and social prospects and to the Bank's past and future role in providing assistance to help resolve Mexico's longer term problems. Mr. McNamara assured President Lopez Portillo that the Bank is prepared to provide Mexico with as much support as possible to finance development projects. He did not wish to specify the magnitude of future lending as this would depend on the number of projects which could be identified and carried out. However, as Bank lending in the past had reached approximately US\$300 million a year, it could be expected that this volume might be increased in response to Mexico's development efforts. In order to reach a satisfactory level of lending, it would, however, be necessary to: clarify the status of some loans which had been approved recently; obtain a definition from the Mexican authorities on other loans which are being

negotiated and, more importantly, agree on a pipeline of projects for future years. The latter would be the only way of ensuring that Mexico might receive a continuous flow of financial assistance from the Bank.

Mr. McNamara said that it would be both to the Government and the Bank's advantage to obtain, as soon as practicable, the Government's decision on three signed loans (SICARTSA II, Rio Bravo Irrigation and the Highways Project). The Bank would be willing to re-examine the nature of these projects but, as Mexican officials -- including the President himself who at one time was a Governor of the Bank -- are aware, there are limitations to the flexibility with which Bank resources may be used. It is not possible for borrowers to use funds granted by the Bank for one project to finance another without first cancelling the unutilized balance available for the first project and analyzing the second independently.

Regarding the loans proposed for five new projects and for which total Bank lending amounting to about US\$250 million has been discussed (Ports II, Maternal-Child Health Care and Family Planning, Urban Development, Rural Development and Baja California Tourism) Mr. McNamara said that it would also be desirable if the Mexican authorities defined their position regarding each project as soon as practicable. He said that he did not wish to let too much time elapse without the Bank granting new loans and disbursing additional funds to Mexico, as this might be interpreted at some future time in the sense that the Bank had not provided support while Mexico was facing difficult circumstances. He suggested that it might be advisable for the Mexican authorities to establish a working group to identify and prepare new development projects which the Bank might finance.

Mr. McNamara then referred to the need for Mexico to increase its internal savings by increased taxation, by improvements in its fiscal systems and/or by adequately pricing the services which the Government provides. Mr. McNamara added that he was aware of the efforts the new administration was making to reduce the fiscal deficit to reasonable limits and that he appreciated that time was required to reach decisions on investment programs. He added that the Bank is prepared to cooperate with the Mexican authorities in analyzing public sector investments and that the authorities could count on Bank personnel for this task; a Bank mission could be sent whenever the Government thought convenient.

In Conclusion, Mr. McNamara said that, in his opinion, the oldest and most difficult problems faced by Mexico are the absence of systematic planning of public investment and scarce, and at times insufficient, fiscal revenues. If Mexico can retain the confidence of the international financial community it could resolve its short-term problems. These, however, should not distract the attention of the authorities from longer

term development problems. Mr. McNamara asked President Lopez Portillo to advise the Bank, as soon as practicable, of his Government's decisions regarding investment priorities and the projects mentioned earlier.

President Lopez Portillo thanked Mr. McNamara for the frankness of his comments and said that he had, for the first time during his visit, been placed on the defensive. There was no doubt that the Bank had clearly demonstrated its interest in helping Mexico; it was now up to the Mexican authorities to resolve pending issues and to create conditions which would make it possible to prepare a pipeline of projects. The President only referred to one of the three approved projects mentioned by Mr. McNamara; he said that SICARTSA II is being re-examined in the light of the private sector's present situation. He added that Mr. de la Madrid would continue the discussions started by the Secretary of Finance, Mr. Moctezuma, with the Bank regarding the five pending loans and the preparation of a pipeline for future loans.

There was then a brief exchange of views in which the Secretary of Tourism (Mr. Rossell de la Lama), the Secretary of Commerce (Lic. Fernando Solana) and Mr. Alfredo Phillips of the Bank of Mexico participated. The Secretary of Tourism expressed his thanks for the way the Bank had cooperated in preparing the Baja California tourism project and expressed interest in obtaining additional Bank support for a tourism credit project. Mr. Solana referred to a possible sector loan for industry and Mr. Phillips briefly sought IFC's assistance in the energy field in light of its new policies. In reply, Mr. McNamara said that it would be advisable to clarify the Bank's position from the beginning on these matters so as to avoid mistaken expectations on the Mexican side about the nature of assistance which the Bank could provide. It was agreed that Mr. de la Madrid and some of his colleagues would meet Mr. Krieger in the afternoon to discuss on which bases loans for tourism and industry might be prepared.

In closing the meeting, President Lopez Portillo thanked Mr. McNamara again for the understanding which he and the Bank had shown toward Mexico while it was facing difficult problems and assured Mr. McNamara that he had no doubts about the extraordinary good will which Bank officials had towards his country.

cc: Messrs. McNamara  
Knapp  
Lerdau  
van der Meer  
Holsen  
Dutt

List of Officials Present at the Meeting  
Between the President of Mexico and Mr. Mcnamara

Lic. Lopez Portillo, President of United Mexican States

Lic. Fernando Solana, Secretary of Commerce

Lic. Rossell de la Lama, Secretary of Tourism

Lic. de la Madrid, Subsecretary of Finance

Lic. Rafael Izquierdo, Advisor to the President

Lic. Alfredo Phillips, Director of International Relations,  
Bank of Mexico

PARTICIPANTES EN LA REUNION CELEBRADA EL  
17 DE FEBRERO DE 1977 ENTRE EL PRESIDEN-  
TE DE LOS ESTADOS UNIDOS MEXICANOS Y EL  
PRESIDENTE DEL BANCO INTERNACIONAL DE  
RECONSTRUCCION Y FOMENTO

Lugar: Blair House  
Washington, D.C.

Sr. Lic. Santiago Roel	Secretario de Relaciones Exteriores
Sr. Lic. Eduardo Pesqueira	Director Ejecutivo - Banco Interna- cional de Reconstrucción y Fomento
Sr. Lic. Fernando Solana	Secretario de Comercio
Sr. Lic. José López Portillo	Presidente de los Estados Unidos Mexicanos
Sr. Lic. José Juan de Olloqui	Subsecretario de Relaciones Exteriores
Sr. José Ramón López Portillo	Hijo del Presidente de México
Sr. Lic. Antonio Enríquez Savignac	Subsecretario de Turismo
Sr. Arq. Guillermo Rossel de la Lama	Secretario de Turismo
Sr. Lic. Alfredo Phillips Olmedo	Subdirector del Banco de México, S.A.
Sr. Lic. Rafael Izquierdo	Asesor del Presidente López Portillo
Sr. Robert S. McNamara	Presidente del Banco Internacional de Reconstrucción y Fomento
Sr. Lic. Hugo B. Margáin	Embajador de México ante la Casa Blanca
Sr. Adalbert Krieger	Vicepresidente - Departamento de Latino- américa y el Caribe en el Banco Interna- cional de Reconstrucción y Fomento
Sr. Lic. Miguel De la Madrid Hurtado	Subsecretario de Hacienda y Crédito Público
Sr. Lic. Adrián Lajous Martínez	Director General del Instituto Mexicano de Comercio Exterior

The above are listed per sitting arrangements.



I have for you  
Public sector deficit 8.32% 62'77  
Limit not on income 8.32  
Official interest reports (182 pc) & income (122 pc)  
Budget with  
Long-term restructuring

CONFIDENTIAL

February 14, 1977

**DECLASSIFIED**  
**MAY 07 2013**  
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Population (196.52.795.58)  
Public orgs - (196.52.795.58)  
revenue (taxes, profits, savings)  
Rising productivity  
rural poor

MEXICO: Briefing for Mr. McNamara's meeting with President Jose Lopez Portillo on February 17, 1977 - Supplementary Notes

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1. This note supplements the briefing papers dated February 8, 1977 for Mr. McNamara's meeting with the Finance Minister Moctezuma. Attached are:

- (i) a biographical sketch of Mr. Lopez Portillo;
- (ii) summary records of the Moctezuma meeting of February 9, 1977;
- (iii) an updating statistical sheet; and
- (iv) copy of letter to Mr. McNamara seeking Bank assistance for Family Planning--representing a sample of letters preceding appraisal of projects.

Ex 78 - Feb 58  
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ing?  
Needs Plan  
for Public  
Investment  
we would  
help

2. Mr. Lopez Portillo's party includes the Secretary of Commerce (Lic. Fernando Solana), the director of Foreign Trade Institute, Mr. Adrian Lajous (former ED of the Bank), and the Secretary for Tourism (Architect Guillermo Rossell de la Lama); his program includes a meeting with Commerce Secretary Kreps suggesting that he will seek from President Carter greater access to the US market for trade and tourism. Meetings are scheduled with Katharine Graham, James Reston and Washington Star, besides a lunch at the National Press Club, and live TV and radio coverage of a press conference, and the visit seems to be a major exercise in public relations with the Americans. Lopez Portillo has also scheduled meetings with Treasury Secretary Blumenthal and heads of IMF, World Bank, IDB, OAS; economic issues--bilateral as well as multilateral--should be prominent on his agenda. The revised program schedules the meeting with Mr. McNamara on the last day of the State visit, and that should offer an opportunity to learn the sum total of Lopez Portillo's assessment of the visit, the economic accommodation he expects from the financial community and the degree and type of support he would want from our institution.

Economy

3. The attached statistical sheet suggests that if the Government succeeds in adjusting the budget as it has proposed, it should meet the Fund target of reducing public sector deficit to 6% of GDP in 1977 compared to 8.3% in 1976, and also manage with the target ceiling of US\$3 billion on net foreign borrowings. (The presently projected current account B/P deficit

is US\$2.5 billion; thus they may not even require the full ceiling amount). The EFF Program extends up to 1979, covering one half of Lopez Portillo's term of office. While plans to implement the main targets for 1977 are reassuring, this is only the first year of a three-year program to reestablish financial stability. The table below presents some of the key EFF targets for 1978 and 1979 along with the actuals for 1976 and revised projections for 1977.

MEXICO: Economic Indicators and EFF Targets

	<u>1976</u>	<u>1977</u>	<u>1978</u>	<u>1979</u>
	<u>Percentage annual rate of change</u>			
Real GDP	2.0~2.5 (4.0)/1	2.0~2.5 (5.0)/1	6.0	7.0
	<u>In percent of GDP</u> (current prices and exchange rates)			
Balance of Payments				
Current Account deficits	4.4	3.5	3.1	2.6
Public Sector Deficit	8.3	6.0	4.0	2.5
Fixed Investment	23.0	24.0	25.0	26.0
a) Public	(8.7)	(8.3)	(8.0)	(8.0)
b) Private	(14.3)	(15.7)	(17.0)	(18.0)
Financing of Fixed Investments	23.0	24.0	25.0	26.0
a) Public savings	(0.5)	(2.3)	(4.0)	(5.5)
b) Private savings	(17.6)	(18.1)	(17.9)	(17.9)
c) External capital inflow	(4.9)	(3.6)	(3.1)	(2.6)

*PSJ  
due 3.5%*

*8.3 → 6.0*

*(0.5) → (5.5)*

*(4.9) → (2.6)*

/1 Assessment when the EFF program was prepared in September 1976

*that resources from private banking etc that flows to restructure debt*

4. Rate of growth of GDP in 1976 and 1977 will be well below population growth (about 3.5% a year) and also below the originally programmed figures of 4 to 5 percent. Even without the mounting concern about illegal immigrants in USA, it is doubtful whether Lopez Portillo could afford to continue this trend for long. He will undoubtedly seek cooperation of the USA and of the international agencies to realize higher growth rates. For attaining the growth projections in the program, the Mexicans would need:

- to enter the US market more effectively, the balance of payments projections in the table (para. 3) assumes real annual growth rates of 14% for exports, 18% for manufactured exports and 12% for tourism (US accounts for 90% of foreign tourists), ambitious targets that could be realized only with substantially improved performance of Mexicans and the cooperation of US industry, importers and travel agents;
- continued access to private banking capital for rollover of old and arrangements for new loans (please see para. 5 on debt management), and understandings with the IMF and Bank that maintain confidence of the private banks in the Mexican economy;
- domestic measures that make it possible for the private sector to increase its share in a growing investment package from about 60% in 1976 to 70% in 1979, and dramatically increase public sector savings from 0.5% of GDP in 1976 to 5.5% of GDP in 1979. Also, while in the past, a part of private savings was utilized to finance public investment, in 1978 and 1979 the private sector savings will roughly equal private investment, and the public investment will, in the aggregate, require to be financed by the sector's own savings plus external capital inflows.

Mr. Lopez Portillo has been saying that Mexico's problem is basically one of the undermanagement of its resources, and has promised to improve the economic management demonstrably. In the short-run better management could solve only part of the problem, namely of reducing the public deficit and perhaps of improving the climate for exports, but Mexico would need substantial foreign borrowings in addition, to be able to maintain, after servicing its foreign debt, the projected level of investment.

#### Foreign Debt

5. At the end of 1976 public sector external debt (including short term debt) is estimated to have been US\$20 billion. It has grown especially rapidly in the last three years; at the same time the terms on which the new debt was contracted considerably worsened (in 1976 the average maturity of medium and long term loans was only 3.5 years). The composition of debt, with short term debt representing more than 20% of the total, makes debt management one of the most critical aspects of economic management.

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- 4 -

6. Our projections show that debt service ratio will peak at 0.48 in 1978 and 1979 and that the share of public sector interest payments (on medium and long term debts) in total exports will be 0.19 in 1978 and 0.17 in 1979. Both indicators are large by any standards, and will constitute a constraint on growth. The magnitude of this constraint becomes even more dramatic if interest payments on public short term debt and private debt were also considered, in which case the interest payments coefficient climbs to 0.23 in 1978 and 1979.

7. For 1977 the amortization payments are estimated around US\$1.74 billion and interest payments US\$1.40 billion. Given a current account deficit of US\$2.50 billion, the gross foreign borrowing are estimated at US\$4.24 billion (1.74 + 2.50); in addition short term debt of about US\$4 billion will need to be rolled over. (Other capital account transactions such as desired private investment and reserve changes are assumed to offset one another.) The problem is being accentuated as some of the private borrowers (e.g. FUNDIDORA steel plant) are finding it difficult to service debts, and the private banks are now insisting on Government guarantee or participation, for any new accommodation.

8. The situation is difficult. An important positive factor is that the outlook for PEMEX increasing its oil exports are good; Reuters in a recent despatch reported that PEMEX exports would increase from 100,000 barrels a day at present to 1 million barrels a day by 1982, corresponding to export earnings of about US\$4.4 billion a year at \$12 a barrel. Rebuilding and maintaining creditors' confidence in the management of the economy is essential since Mexico will be dependent upon the continuing cooperation of the private banks.

9. Mr. Pesqueira in a recent despatch to the Finance Minister (copy made available to the staff by his courtesy) drew the Government's attention to the dangers of the heavy dependence on the Eurodollar market and private banks, borrowing at floating interest rates linked to LIBOR (those rates are fortunately low for the present), and recommended that, to the extent possible, Mexico should shift to borrowings from institutions such as the Bank, IDB and external credit agencies (EXIM, KfW, etc.).

10. The importance of restructuring its foreign debt cannot be over-emphasized. This can be accomplished, however, only over a period of years by simultaneously reducing the level of net borrowings and maximizing the use of financing from official and credit institutions. Mr. McNamara may wish to suggest that President Lopez Portillo give special importance to this subject and ask for a strategy to be prepared; to the extent possible the Bank would assist with technical assistance and financial assistance (including co-financing) of Government's priority investments. Mexico has competent economists and should be able to do most of the work on its own; the Bank staff could be of assistance in analyzing the public investment program, in identifying areas where foreign finance could be available, and help in maintaining the confidence of the financial community in Mexico by preparing objective Economic Reports. At the invitation of the national

electricity organization, CFE, we are organizing a mission for April 1977 to analyze the sector. While our own economic work program for Mexico must continue to include short-term economic management, we expect to devote increasing attention to the medium-term public sector investment program and its financing.

11. To summarize the discussions on the economy, Mr. McNamara may wish to compliment the President on the several achievements in the relatively short period of his administration. The trends look promising, but Mexico faces considerable difficulties in foreign debt management, containing inflation and resuming economic growth in per capita terms. The Bank looks forward to continuing its intimate relationship with Mexico, and will be happy to assist in preparation of a program that enables it to move through a period of stabilization to growth, and in implementing it.

#### Operational

12. On the operational side there is little new to add to the briefing note of February 8, and the subsequent discussions with Finance Minister. The table below presents some figures on Bank exposure in Mexico:

	<u>No. of Loans</u>	<u>Amount (US\$ million)</u>
Total	<u>47</u>	<u>2,631</u>
- Agriculture, Rural Development	14	906
- Industry	6	310
- Power	12	715
- Water Supply	2	130
- Transport	12	548
- Tourism	1	22

The first Bank loan to Mexico was made in January 1949, for power to CFE, and now with \$2.63 billion, Mexico is one of the largest borrowers from the Bank. Of this total around \$1.75 billion were borrowed by the Echeverria Government in the last six years. Of the total loan amount of \$2.63 billion so far committed, \$1.65 billion have been disbursed; the rate of disbursement has accelerated from about \$7 million a month in the period January-November 1976 to \$24 million a month since then. Responding to Government's request (a sample of letters addressed to Mr. McNamara is attached), we have appraised five projects, and, as concluded in the meeting with Finance Minister Moctezuma (summary record--attachment II), Government's decision to proceed with those projects would be awaited for finalizing those loans. Perhaps it may be worth informing Mr. Lopez Portillo that any slowing of operations should not be construed as lack of Bank's sympathy for Mexico in its present period of difficulties.

#### Attachments

LAC Region  
February 14, 1977

**NACIONAL FINANCIERA, S. A.**

APARTADO POSTAL N° 353 ISABEL LA CATOLICA N° 51

TELS. 5-18-15-28 Y 5-18-16-80

CABLE: 'NAFIN'

MEXICO I. D. F.

DIRECCION GENERAL

*Reyes - Family Planning*

2409

November 3, 1976.

Mr. Robert S. McNamara  
President  
International Bank for Reconstruction  
and Development  
1818 H. Street, N. W.  
Washington, D. C., 20433  
U. S. A.

Dear Mr. McNamara:

*Nacional Financiera, S. A., on behalf of the Federal Government of the United Mexican States, and acting as its financial agent, hereby formally requests from the International Bank for Reconstruction and Development a loan which will be used to partially finance a National Maternal-Child Welfare Program and Family Planning. The Program will be executed by a Group integrated by Secretaría de Salubridad y Asistencia, Instituto Mexicano del Seguro Social, Instituto de Seguridad y Servicios Sociales de los Trabajadores del Estado and acting as technical advisor the Consejo Nacional de Población, all them coordinated by Secretaría de la Presidencia.*

*The subprograms, which form part of the National Program, consist of the following parts: a) Maternal Health Program, b) Child Health Program, c) Voluntary Family Planning and, d) Maternal-Child Health Orientation Program.*

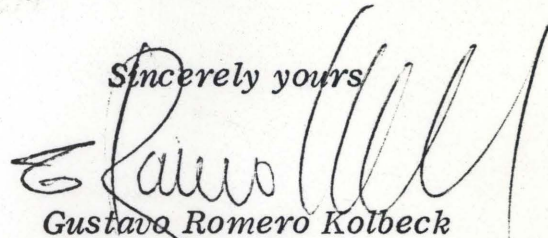
*We hope to have the opportunity to exchange views, as soon as possible, with officials and technicians of the Bank in order to discuss the details of the project, since that Institution has already extensive technical information concerning the National Program.*

...

We are leaving open for discussion the amount of the loan, as well as the related financial conditions but as always we hope to obtain the best possible terms.

We will deeply appreciate your attention to this request, and hoping to hear soon from you, I remain.

Sincerely yours



Gustavo Romero Kolbeck  
Director General

- C.c.p. Sr. Lic. Mario Ramón Beteta, Secretario de Hacienda y Crédito Público, Palacio Nacional, Ciudad.
- C.c.p. Sr. Lic. Ignacio Ovalle Fernández, Secretario de la Presidencia, Palacio Nacional, Ciudad.
- C.c.p. Sr. Dr. Ginés Navarro Díaz de León, Secretario de Salubridad y Asistencia, Oaxaca No. 58, México, D. F.
- C.c.p. Sr. Lic. Jesús Reyes Heróles, Director General, Instituto Mexicano del Seguro Social, Paseo de la Reforma 476 - 1er. piso México 6, D. F.
- C.c.p. Sr. Lic. Salvador Sánchez Vázquez, Director General, Instituto de Seguridad y Servicios Sociales de los Trabajadores del Estado, Av. Juárez 154, 1er. piso, México 1, D. F.
- C.c.p. Sr. Lic. Miguel de la Madrid Hurtado, Subsecretario de Hacienda y Crédito Público, Secretaría de Hacienda y Crédito Público, Palacio Nacional, Ciudad.
- C.c.p. Sr. Lic. Víctor Navarrete R., Director General de Crédito, Secretaría de Hacienda y Crédito Público, Moneda No. 4, 2° piso, Ciudad.
- C.c.p. Sra. Lic. Luisa María Leal, Secretaria General, Consejo Nacional de Población, Paseo de la Reforma No. 136, Piso 16, México 6, D. F.
- C.c.p. Sr. Lic. David Ibarra M., Subdirector General, Nacional Financiera, S. A., Edificio.
- C.c.p. Sr. Lic. Pedro Galicia E., Gerente General de Operaciones Internacionales, Edificio.
- C.c.p. Sr. Lic. Fernando Torres V., Jefe de la Oficina de Nacional Financiera en Washington, D.C. 20036, E. U. A.
- C.c.p. Sr. Lic. Agustín Valdés C., Gerente de Proyectos Internacionales, Presente.

Jose LOPEZ PORTILLO y Pacheco  
President of the United Mexican States  
Biographical Note

1. Mr. Lopez Portillo was born on June 16, 1920 in Mexico City, but he comes from a distinguished Guadalajara family which traces its roots back 400 years to northern Spain. His father was a prominent historian who died about two years ago. As a child, Mr. Lopez Portillo went to state-run school with Mexico's previous president, Mr. Echeverria, with whom he also studied law at the National University at Mexico City. After graduation, Mr. Lopez Portillo practiced law and taught this subject as well as political science and public administration at the National University until, at the age of 39, he accepted his first post in the Government as Advisor to the Secretary of Patrimony. When President Diaz-Ordaz took office in 1965 Mr. Lopez Portillo became Director of Legal Affairs at the Secretariat of the Presidency, later rising to Undersecretary and carrying out major administrative reforms. When Mr. Echeverria assumed the Presidency, Mr. Lopez Portillo was appointed Undersecretary of National Patrimony and in 1972 head of CFE, the Government-owned power company and, at the time, one of the Bank's largest borrowers. After nine months in this post he was appointed Secretary of Finance, which office he resigned in early 1976 after being selected to be the Government Party's candidate for the Presidential election.

2. Though close to ex-President Echeverria, Mr. Lopez Portillo's style and outlook may turn out to be quite different from his predecessor's. Mr. Lopez Portillo is impatient with verbosity and rhetoric and has a down-to-earth approach to issues. He has brought a conciliatory mood to government, and has quietly taken steps to mend the rift between Mexico City and the private sector groups of Monterrey, which was partly created by Mr. Echeverria's inflammatory speeches against business interests during his last months in office. Mr. Lopez Portillo has the reputation of being a "technocrat" (which description he does not like) and is greatly concerned about efficiency, organization and productivity. During his campaign, he repeatedly stressed the importance of simplifying public administration to make it more efficient and of eliminating corruption in public office. One of his first steps as President was to reorganize public administration, giving responsibility for selecting sectoral priorities and formulating policies to a few secretariats in order to do away with the confusion which resulted from duplication of functions among a large number of organization created by previous administrations. He also transformed the Secretariat of the Presidency into the Secretariat for Planning and Budgeting in order that long term programs be evaluated systematically and programmed in relation to forecast resources. Up to then, the budgetary process, which only looks ahead one year, was the only means by which the Government could attempt to



gauge the magnitude of total expenditures and investments. Mr. Lopez Portillo named Mr. Carlos Tello, who is well-known to the Bank, to head the new Secretariat for Planning and Budgeting.

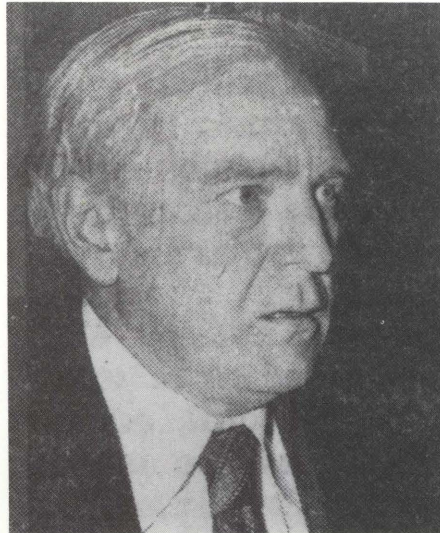
3. Mr. Lopez Portillo has written two novels as well as two books on political theory. He has a sense of humor and enjoys good food and wine. Classical music and physical exercise -- karate -- are two of his favorite pastimes. He understands English well but prefers to speak in Spanish.

Adrián LAJOUS Martinez  
(Phonetic: laHOOS)

MEXICO

Director General, Mexican  
Foreign Trade Institute  
(since 1 December 1976)

Addressed as:  
Mr. Lajous



In his new position, Adrián Lajous is responsible for the promotion of Mexican foreign trade. A bright man experienced in banking and international commodities, he is also a professor of economics at the Center for Economic and Demographic Studies of the Colegio de Mexico, a highly rated graduate school in the social sciences and humanities. From at least November 1975 until December 1976, Lajous served as director general of the *Fondo de Equipamiento Industrial*, a government fund that provides credits to create and modernize business enterprises that produce export products or import substitution products.

Sometime prior to 1960, Lajous was Minister-Counselor of Embassy in Washington, D.C. He visited the United States in 1967 to serve as interpreter for President (1964-70) Gustavo Díaz Ordaz and in 1976 to participate in a seminar on Mexico sponsored by American University in Washington, D.C. Lajous has been a representative to several international commodities organizations, including the International Coffee Organization and the International Sugar Council, both in London. During 1972 he was the International Bank for Reconstruction and Development director for Mexico and Central America. He attended the 1973 UN Conference on Sugar, held in Geneva, and headed its Economic Committee. Lajous' abilities have earned him the high regard of his fellow delegates to international meetings.

Lajous is fluent in English and French. He is married; his wife is the sister of Enrique Loaeza Tovar, the director general of airports and auxiliary services.

CR M 77-10449  
2 February 1977

Fernando SOLANA Morales  
(Phonetic: soLAna)

MEXICO

Secretary of Commerce  
(since 1 December 1976)

Addressed as:  
Mr. Secretary



A former journalist with some experience in the field of finance, Fernando Solana was appointed Secretary of Industry and Commerce on 1 December 1976. He became Secretary of Commerce in January 1977 upon the reorganization of the Secretariat. He will oversee and coordinate the activities of such state-owned firms as the Mexican Tobacco Institute; the Mexican Foreign Trade Institute; the National Foreign Trade Bank; the National Sugar Producers' Union (UNPASA); and the National Corporation for Popular Subsistence (CONASUPO), the government agency for controlling the price and distribution of basic commodities.

Solana worked on various magazines and newspapers in Mexico City during 1952-66. In 1961 he became an adviser on international economic problems at Nacional Financiera, S.A., the national development bank that is a lending institution owned jointly by the Government of Mexico and private individuals. During 1964-66 Solana was an adviser to UNPASA. Concurrently during 1965-66 he was a member of the public administration commission of the Secretariat of the Presidency. A member of the Directive Council of the National Center for Productivity during 1966-70, Solana then became subdirector of CONASUPO, a post he held until 1976.

The holder of degrees from the National Autonomous University of Mexico (UNAM) in civil engineering (1952), philosophy (1955) and political science and public administration (1963), Solana lectured in journalism, political science and economics at UNAM during 1962-75 and served as its secretary general during 1966-70. He has traveled to Peru, Chile and the United States.

CR M 77-10463  
4 February 1977

Latest Available Statistical InformationStatistical Annex

	<u>1976</u>	<u>1977</u> (expected based on latest analysis)
<u>Growth</u>		
GDP (in %, real terms, compared with preceding year)	2.0-2.5	2.0-2.5
<u>Balance of Payments</u>		
Deficit on the current account		
- in \$ billion	3.4	2.5
- in % of GDP	4.4	3.5
<u>Public Sector Finances</u>		
Deficit of the public sector (including public enterprises)		
- in billions of current pesos	102.2	144.7 (budgeted)
		Adjustment expected from new programs: expenditure cuts - 15.0
		implemen- tation of price adjust- ments - 7.8
		new revenue - 19.0
		102.9 (resulting from implementation of new programs)
- in constant 1976 prices	102.2	107.2 (budgeted) 76.2 (after program implementation)
- as % of the GDP	8.3	8.5 (budgeted) 6.0 (after program implementation)
<u>Prices</u>		
Consumer price index (%)	27.5	35.0
<u>Foreign Reserves</u>		
- US\$ billion		1.1 (February 1977)
- in months of imports		1.3

100% COTTON FIBRE  
BOND  
MADE IN AUSTRIA



## OFFICE MEMORANDUM

CONFIDENTIAL

DECLASSIFIED

DATE: October 4, 1977

MAY 07 2013

WBG ARCHIVES

TO: Memorandum for the Record  
 FROM: Devbrat Dutt, *D. Dutt* Division Chief, LAC IA  
 SUBJECT: Meeting of Mr. McNamara with the Mexican Delegation on September 29, 1977

1. Mr. McNamara met with Mr. Julio Rodolfo Moctezuma Cid, Finance Minister, on September 29, 1977. Mr. Moctezuma was accompanied by Messrs. Gustavo Romero-Kolbeck (Director General of the Bank of Mexico), David Ibarra (Director General of Nafinsa), Mr. Gilberto Escobedo (Director of Public Credit in the Ministry of Finance), Mr. Eduardo Pesqueira (Executive Director for Mexico), and several of their advisers. Also present were Messrs. Knapp, Krieger, Lari, Holsen and Dutt.

2. Mr. Moctezuma opened the meeting with an acknowledgment that the project pipeline for borrowing from the Bank had been weak in the past and stated that President Lopez Portillo had carried a strong impression of his meeting with Mr. McNamara (the Minister said that the President was 'put to shame' because of lack of projects) and had instructed his staff to strengthen the pipeline. Accordingly, the Government has in recent months improved their internal mechanism for project preparation and has now submitted to the Bank several projects of major interest to Mexico, and he was pleased to learn from Mr. Krieger that the Bank was processing them expeditiously. Mr. Moctezuma assured Mr. McNamara that decisions on the remaining pending issues would be taken shortly and he looked for an active relationship between Mexico and the Bank. Mr. Moctezuma then explained the several improvements in the economic situation, and in an apparent reference to Mr. McNamara's response to the Latin American Caucus the previous day, stated that his delegation was particularly encouraged by Mr. McNamara's position on assisting developing countries in their energy and oil programs. He had given considerable thought to possible Bank assistance to Mexico in this critical area and came to the conclusion that because of the complexity in dealing with PEMEX, it would be preferable to seek the assistance of the Bank in developing the capital goods industries that would supply PEMEX with machinery, equipment, storage tanks, pipes and other items to enable it to carry out its sizable investment program; for several of these items there is some manufacturing capacity in Mexico, but this requires expansion and he requested Mr. McNamara to consider a line of credit, somewhat on the lines of FONEI operation but separate from the forthcoming FONEI III operation. Mr. Moctezuma said that if Mr. McNamara was sympathetic he would make a formal presentation. The Minister also requested the resumption of lending to CFE and stated that a financial rehabilitation plan for CFE has been prepared. Mr. Moctezuma assured Mr. McNamara that within a short time the project pipeline would be further strengthened.

3. Mr. McNamara said that he was not satisfied with the Bank lending program for Mexico, the amounts were less than Mexico needs, and some of the projects were not as strong as we would like them to be. He stated that, while we were satisfied with the rural development program, there were several others which were either being modified or cancelled. He would like to see a substantial expansion in lending to Mexico and for that a solid program as well as continued efforts to tackle the more serious economic problems would

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be necessary. Fundamental problems of Mexico were development of the rural areas, creation of employment opportunities and debt management, and clearly the savings efforts of Mexico had to be improved to provide a better base for its considerable investments. Mr. McNamara suggested that a picture be presented explaining (a) the total investment program for the medium-term, (b) a medium-term Bank lending program, and (c) the priority of the proposed capital goods project within the above two; he would wish to take a decision against the background of such an analysis. Mr. McNamara assured the Minister that he was not opposed to the capital goods project, but in the interest of Mexico itself would not wish to present such a project to the Executive Directors without a solid base.

4. Mr. Moctezuma admitted that the project pipeline was weak in the past, but it was being improved and assured Mr. McNamara that the capital goods project had a sound rationale. Mr. David Ibarra intervened to explain a possible misunderstanding on the pipeline; he said that the projects for the next few years were rather well defined and the main thrust was for:

- Agriculture and social development;
- Small and Medium Industries for job creation and to promote decentralization of economic activity;
- Support to fundamental areas such as petroleum and capital goods.

Mr. Krieger stated that capital goods industry was weak in Mexico and needed development both on employment and balance of payments considerations. He also explained that we were proposing to send a mission to Mexico in the coming months to review the findings of the economic mission, and that would be an occasion for further discussion on the Mexican Administration's mid-term investment program.

5. Mr. McNamara said that the Mexican proposal was essentially a program loan for capital goods industries, and this must rationally fit in the Bank's enlarged lending program. He assured the Minister that we would want to be associated with the Government's program, and requested for information on the medium-term investment plan so as to understand the justifications for the project in the larger context of Mexico's investment efforts and Bank's own support to Mexico. He thought that lending to Mexico could become very large, larger than for any other country perhaps excepting Brazil.

6. Mr. Moctezuma thanked Mr. McNamara for the economic work in the country and said that they had greatly appreciated the analysis and advice of the economic missions and President Lopez Portillo had been impressed by the presentation of Mr. Villarzu; the papers prepared in the Bank on the Mexican economy had been greatly valued in Mexico and had proved to be highly productive. The Minister added that the Government had complied with the Fund requirements. Mr. McNamara congratulated the Government on the excellent performance of the previous months and requested him to convey these compliments

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to the President. He stated that he had read the text of the IMF Agreement and had followed with great satisfaction Mexico's performance which had successfully met the IMF's conditions.

7. Referring to the New York Times story of that morning, Mr. McNamara queried the Minister about Mexico's intention to carry out a family planning program and the role of the Bank in such a program. Mr. Moctezuma stated that Mexico was determined to carry out a program for reducing growth of population and that since the family planning project was appraised by the Bank several institutional changes have taken place (the responsibility has been shifted from IMSS, Mexican Institute of Social Security, and ISSSTE, Social Security Institute of Government Employees, to the Ministry of Health). He said that he would wish to guarantee a solid population program, but, given the number of institutions still involved in this field, he was not yet in a position to indicate whether such a program would be financed entirely by domestic resources, or partly by the Bank. A decision in this regard would be taken shortly.

8. In closing the discussions, Mr. McNamara stated that we would be responding to Mexican wishes and requested the Minister to convey his greetings and congratulations to President Lopez Portillo.

cc. Mr. McNamara's Office

Messrs. Knapp, Krieger, Lari, van der Meer, Holsen

DDutt.vb